TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, [redacted] 1925

No. [redacted] 67

BURK-WAGGONER OIL ASSOCIATION, PLAINTIFF IN ERROR,

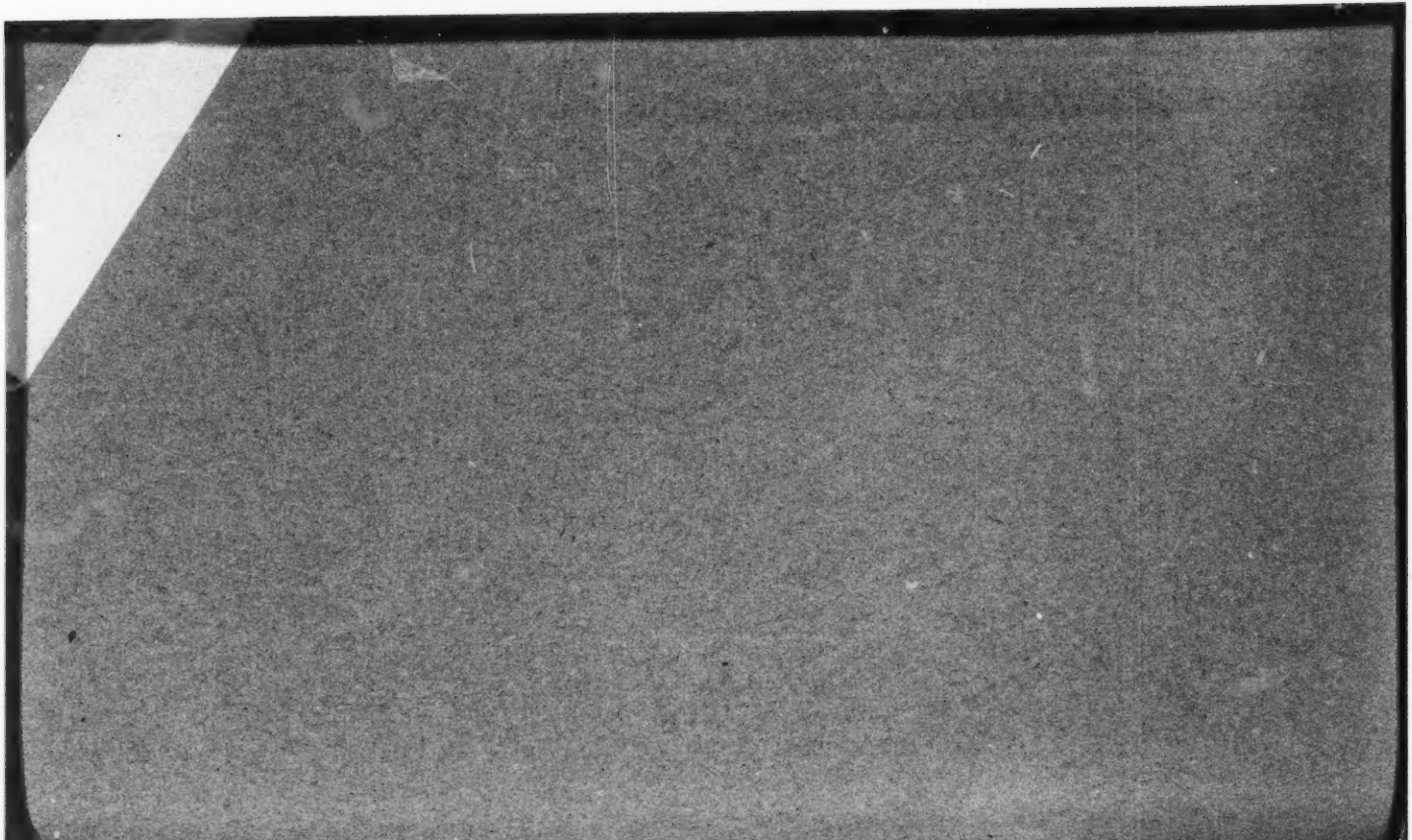
vs.

GEORGE C. HOPKINS, COLLECTOR OF INTERNAL REVENUE, SECOND DISTRICT OF TEXAS

IN ERROR TO THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF TEXAS

FILED MAY 20, 1926

(30,353)



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INDEX

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., JANUARY 8, 1925

[fol. 1] CAPTION—Omitted

[fol. 2] **IN UNITED STATES DISTRICT COURT**

PLAINTIFF'S SECOND AMENDED ORIGINAL PETITION—Filed Feby. 21, 1924

o the Hon. Wm. H. Atwell, Judge of said Court:

Now comes the plaintiff, Burk-Waggoner Oil Association, and, ave of the Court being first had and obtained, files this, its Second mended Original Petition, in lieu of its Original Petition hereto- ore filed in this cause, and for such amended petition alleges:

That the plaintiff, Burk-Waggoner Oil Association, is an unin- orporated association or partnership with its office and place of usiness in Wichita Falls, Wichita County, Texas, and the defend- nt, Geo. C. Hopkins is a resident of Dallas County, Texas, and is, nd was at all the times hereinafter mentioned, the duly and legally ppointed, qualified, and acting Collector of Internal Revenue for ie Second District of Texas;

That the amount involved in this controversy exceeds, exclusive interest and costs, $3,000.00, and arises under the Constitution the United States and under the laws relating to internal revenue will more fully appear hereafter.

Plaintiff would show to the Court that during the year of 1919 was engaged in the business of producing oil in the oil fields of Vichita County, Texas, and for that purpose employed a capital of 60,000.00 contributed by its members. That from its operations nd the sale of its property said association or partnership received [fol. 3] a profit amounting to $1,838,053.90, in the year 1919.

That during the year of 1919, and subsequent thereto, the Bureau Internal Revenue of the United States had adopted rules and regu- tions which required, in substance, that enterprises created and xisting as plaintiff was created and existing should pay the tax levied said act upon corporation; that, in compliance with said rules and gulations, and to avoid the penalties and prosecutions which might herwise result, the plaintiff in due course, in the year 1920, filed return or report of its transactions, for the year 1919, which re- rn and report was filed under protest and which showed that said nterprise had made the net profit above shown, to-wit, $1,838,053.90, d plaintiff paid thereon the amount of tax shown to be due by said port, when computed in accordance with the instructions con- ined in said Regulations, upon the following dates and in the llowing amounts:

n March 15, 1920	$138,150.51
n June 12, 1920	138,150.51
n September 12, 1920	138,150.51
n March 28, 1922	145,827.67
A total of	$561,279.20

That the first three payments above mentioned were paid to defendant's predecessors in office, but the last payment was paid to defendant, and it and all other payments were made under protest, and to avoid the penalties and seizure of property which plaintiff was notified by defendant, his predecessors in office, and the published regulations and instructions of the Bureau of Internal Revenue would result if said sums were not paid.

Plaintiff would next show to the Court that this enterprise was created by written contract between several individuals, residents of [fol. 4] Texas, which written contract was styled "Articles of Association." That same was executed on November 15, 1918, and was filed for record with the County Clerk of Wichita County, Texas, on December 27, 1918, and is recorded in Volume 107, pages 579 to 582, Deed Records of Wichita County, Texas. Said Records are hereby expressly referred to and made a part hereof for all purposes. That said enterprise is not incorporated and has no rights or charter granted by the Laws of any State or the United States. That said Articles of Association provided, in substance, that the signers of same and those who may become associated with them should engage in the business of prospecting for, producing and selling crude oil and in kindred enterprises, and that for said purposes a fixed amount, termed capital stock, should be used to be contributed in cash and property by the subscribers to said Articles and those who might become associated with them, that profits were to be shared by those connected with the enterprise in the proportion in which they contributed to said common fund or capital stock, that each one so interested should have a voice in management and control of the same in proportion to his contribution which was to be exercised at meetings of those interested, that the actual management of the enterprise was to be vested in a board of Trustees selected from those interested, and to be re-selected annually by those interested in meetings to be held for that purpose. It was also provided that transferable receipts or certificates of stock were to be issued to those contributing to the enterprise, that neither the transfer of such receipts and the interest represented thereby, nor the death, insolvency or incapacity of the holder thereof should terminate the enterprise.

Plaintiff alleges that said enterprise was conducted as provided for in said agreement and that said enterprise is a partnership, and that it and its members are subject to taxation by the United States [fol. 5] of America, under the Revenue Act of 1918, if at all, under the terms and provisions thereof relating to partnerships and individuals, and not under the terms and provisions thereof relating to corporations, and that no sum whatsoever was due by said enterprise as taxes but any and all profits received from the operations conducted by plaintiff was the income of the various members of said enterprise in an amount proportionate to their interests and that no income or excess-profits tax should have been assessed against or collected from plaintiff.

That, more than six months prior to the time the original petition herein was filed, plaintiff filed with the Collector of Internal Revenue

a Claim for the refunding of all of said sum so paid defendant, based upon the facts herein set forth and for other reasons. That, so far as plaintiff knows, said claim has never been acted upon and plaintiff alleges that if it has been acted upon it has been rejected by the Commissioner of Internal Revenue.

That the collection of said tax from plaintiff is unconstitutional in that it is contrary to the provisions of Article I, Section 1, Section 2, Section 8 and Section 9, of the Constitution of the United States, and also of the Sixteenth Amendment thereto, in that the said tax is not based upon income and is not in proportion to population; and in so far as the collection of the said tax purports to be based upon official regulations, it is unconstitutional in that such regulations are beyond the power of the Secretary of the Treasury to promulgate, and are beyond the power of Congress to authorize.

That the individual members of the plaintiff have, by the said collection, been subjected to unlawful and unconstitutional taxation because such taxation is not authorized by the Revenue Act of 1918, or any other act; and if it be held that such taxation is authorized by the said Act then said Revenue Act of 1918 is unconstitutional and [fol. 6] contrary to the Fifth and Sixteenth Amendments. The taxes hereinabove referred to have been imposed upon the individual members of plaintiff irrespective of their incomes and irrespective of the rates of tax set forth in the said Revenue Act of 1918 and, in so far as they exceed taxes in accordance with the said rates, they are unlawful and unconstitutional.

That because of these facts plaintiff is entitled to have and recover of and from defendant the amount so paid defendant, to-wit, $145,827.67, with interest thereon from the date of payment at the rate of six per cent per annum.

That the acts of defendant in demanding payment of and collecting said sum were done with probable cause and under the instructions of the Commissioner of Internal Revenue.

Wherefore, premises considered, plaintiff sues, prays for service to defendant, and that, upon final hearing hereof, it have judgment against defendant for the sum of $145,827.67, with interest thereon at the rate of six per cent per annum from March 28th, 1922, together with all costs of suit; that a certificate of probable cause be issued by this Court and that plaintiff have such other and further relief as it may be entitled to receive.

Weeks, Morrow & Francis & John M. Sternhagen, Attorneys for Plaintiff, Burk-Waggoner Oil Association.

[fol. 7] IN UNITED STATES DISTRICT COURT

ANSWER—Filed May 18, 1923

Comes now the defendant, George C. Hopkins, Collector of Internal Revenue and demurs to the plaintiffs petition herein and says the same is insufficient in law and shows no cause of action against him, and of this he prays the judgment of the Court.

If required for answer here the defendant denies all and singular the allegations in said petition contained and demands strict proof and of this he puts himself on the country.

Henry Zweifel, United States Attorney, by N. A. Dodge, Special Assist. to the U. S. Attorney, Attorneys for the Defendant.

[fol. 8] IN UNITED STATES DISTRICT COURT, NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION

No. 3301. At Law.

BURK-WAGGONER OIL ASSOCIATION

vs.

GEO. C. HOPKINS, Collector of Internal Revenue

Action at Law for the Recovery of $145,827.67, with Interest

OPINION—Filed March 3rd, 1924

Weeks, Morrow & Francis, Wichita Falls, Texas; Kix, Miller & Baar, Chicago, Illinois; Harry C. Weeks, Wichita Falls, Texas; J. M. Sternhagen, Chicago, Illinois, for the plaintiff.

Henry Zweifel, United States Attorney, Fort Worth, Texas; N. A. Dodge, Assistant United States Attorney, Fort Worth, Texas; Nelson T. Harston, Solicitor of Internal Revenue, Washington, D. C.; Arthur H. Deibert, Special Attorney, Department of Internal Revenue, Washington, D. C., for the defendant.

The plaintiff alleges that it is an unincorporated association or partnership; that its members contributed $60,000.00 as a capital to be used in the business of producing oil in the oil fields of Wichita County, Texas; that in the year 1919 it received a profit on such investment of $1,838,053.90; that the bureau of internal revenue of the United States had adopted certain rules and regulations which required the plaintiff to pay $561,279.20 income tax on said net profit; that such payment was made in four installments, the first three being paid to the predecessors of the defendant against whom suit likewise pends, and the latter, of $145,827.67, having been paid to the defendant; that all of such payments were had under protest [fol. 9] and to avoid penalties and seizure.

Plaintiff contends that the enterprise was a partnership and that its members are subject to tax under the revenue act of 1918, if at all, under the terms and provisions relating to partnerships, and individuals relating to corporations, and that no sum whatever was due by said enterprise as taxes, but that any and all profits received from such operations were the income of the various members of said enterprise in an amount proportionate to their interest, and that no

income tax should have been assessed against, or, collected from the plaintiff.

That the collection of such tax from the plaintiff was unconstitutional and contrary to the provisions of Article 1, Section 1; section 2, section 8 and section 9 of the Constitution of the United States; and, also to the provisions of the sixteenth amendment thereto, in that the same is not based upon income and is not in proportion to population; that in so far as it purports to be based upon official regulations it is unconstitutional in that such regulations are beyong the power of the Secretary of the Treasury to promulgate, and, beyond the power of the Congress to authorize; that the individual members of the plaintiff have been subjected to unlawful and unconstitutional taxation because such tax is not authorized by the revenue act of 1918; that if it be held that such taxation is authorized by said act, then said act is unconstitutional and contrary to the fifth and sixth amendments to the Constitution; that the taxes referred to have been imposed upon the individual members of the plaintiff irrespective of their claims and irrespective of the rates of tax set forth in the act of 1918.

The defendant replied by general demurrer and general denial.

A jury was waived, and from an agreed statement of facts it was shown:

(a) That a written agreement, set out in full in the stipulation, [fol. 10] was executed on the 15th day of November 1918 by R. M. Waggoner, Clois L. Green, Lee Crenshaw, D. H. Melton, W. H. Anchor and A. H. Murchison, which was filed for record in the deed records of Wichita County, Texas, on the 27th day of the next month.

Article one of such agreement provides for the formation of an "unincorporated joint stock association," to be known as "Burk-Waggoner Oil Association," to continue in existence during the lives of the six individuals and for twenty-one years after the death of the one who last dies, unless sooner dissolved. The general purpose of the company was the purchase or lease of lands containing oil, to extract the same and to do all other things necessary or proper, incident to the mining, manufacture, sale or transportation of oil and its products. That the capital stock should be $60,000.00 divided into 600 shares of $100.00 each to be evidenced by certificates. That such certificates should be signed by the board of trustees and countersigned by the secretary; such certificates refer to the plaintiff as a joint stock association, and are transferrable only on the books of the company; that no member of the company, or, owner, or, holder of the certificates shall have any authority, power, or, right to transact any business whatever for, or, on behalf of, or, binding on the company, or any member thereof, and that no member of the company shall be personally liable for any debts, demands, contracts of any kind, or torts of the company, beyond the payment in full of the price for which the share or shares were sold individually by the company; that shareholders should have no right of partition, nor, of dissolution of the trust, but that the shares should be per-

sonal property carrying the right of division of profits, and at the termination of the trust to a division of the principal and profits in proportion to the number of shares held; death, insolvency, or, [fol. 11] bankruptcy of any member, or a transfer of his interest should not work a dissolution nor should it entitle anyone to an action or proceeding in law or equity against the members, trustees, officers or property; the affairs of the company were to be managed by a board of six stock-holding trustees whose successors should be elected annually by a majority of the shares present or represented at a meeting, and each board to elect its own president and other officers and prescribe their duties; title to all property was to be held in the name of the trustees who would hold it as joint tenants and not as tenants in common; such trustees, in their capacity as such, might sue or be sued in any court of law, or, equity, or, the company might sue or be sued in the company name, as provided by the statutes of Texas; trustees had full power and authority to conduct the affairs of the business; in case of a vacancy on the board the remaining members might fill the same, subject to the right of the shareholders to do so, should they see proper to exercise the right; the board would select managers and employees as they were necessary, fixing their compensation and defining their duties; the board to declare and pay dividends as they might deem expedient; that such board should have no power to bind the shareholders or members personally; that in every written contract entered into by the trustees they should refer to the declaration of trust and that anyone contracting with them should look only to the funds and property of the company for the payment of any debt or judgment; neither the trustees nor the shareholders should be personally liable for any debt; the board would adopt such by-laws as it thought proper; any annual special meeting of the shareholders might amend the articles of association by a vote of three-fourths of the shares present and that by-laws might be adopted, repealed or amended in any respect, not inconsistent with the articles, by a vote of two-thirds of the shares present or compensation and defining their duties; the board to [fol. 12] declare and pay dividends as they might deem expedient; that such board should have no power to bind the shareholders or members personally; that in every written contract entered into by the trustees they should refer to the declaration of trust and that anyone contracting with they should look only to the funds and property of the company for the payment of any debt or judgment; neither the trustees nor the shareholders should be personally liable for any debt; the members of the company would be protected from personal liability; the board would adopt such by-laws as it thought proper; any annual special meeting of the shareholders might amend the articles of association by a vote of three-fourths of the shares present and that by-laws might be adopted, repealed or amended in any respect, not inconsistent with the articles, by a vote of two thirds of the shares present or represented; shareholders should meet annually in June to consider the affairs of the company, transact such business as they might inaugurate and as might be submitted by the trustee; the members of the board of trustees were at all

times to be subject to the orders of the shareholders, who might at any time and for any cause, by a vote of majority of all the shares then issued and outstanding, remove any one or all of them from office, and appoint and devolve upon other members the duties and functions of the office. No trustee should be liable for any fraud, or, error, or, negligence of a co-trustee to which he had not been a party, and there was a method provided by which he might relieve himself from liability to the shareholders for any act of the board which he had not approved; $40,000.00 of the capital stock should be paid by conveying to the six trustees an oil and gas lease, the balance of the $60,000.00 was to be paid in cash; the stock of the association could be increased at any time by a vote of the majority of the stockholders present; dissolution could be affected by a vote of three-fourths of the shares, provided there were no outstanding bonds or obligations secured by mortgage of the company's property.

[fol. 13] (b) That the tax collected from the plaintiff in the manner and amount alleged in the petition.

(c) That legal demand had been made for the return thereof as required by the law.

(d) That about two hundred persons were interested and were certificate holders in the association, and the certificates of the assotiation were traded in generally by the public.

1st

The revenue act of 1918, in section one of title one provides, that, "The term 'person' includes partnerships and corporations, as well as individuals; the term 'corporation' includes associations, joint stock companies and insurance companies."

Section 218 of the same act provides, "That individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership of the taxable year * * *."

The latter paragraph of section 335 of subdivision C of the same act reads as follows: "Any tax paid by a partnership or personal service corporation for any period beginning on or after January 1st, 1918, shall be immediately refunded to the partnership or corporation as a tax erroneously and illegally collected."

Without presenting the provisions which relate to the tax to be paid by corporations, associations and joint stock companies, it is manifest from the above provisions that partnerships are to pay the income tax through the persons who compose it, while the corporation, association and joint stock company is to pay the tax as entitles of so many taxable persons; the corporation, association and joint stock company is, itself, the taxable entity or person.

[fol. 14] May an aggregation of individuals be both a partnership and an association; be both a partnership and a joint stock company? If so, how are such individuals to be reached? If the taxable profit be made by a corporation or an association or a joint stock company, then either of the three must pay the tax before the individuals who are entitled to the profits of either receive that which is theirs and after receiving it, it must again be accounted for in such individual income tax return and payment. The profit of a partnership, however, is then and there and at that time the profit of the partner and is taxed as such and not as the profit of any artificial person.

It was clearly the intention of the congress that that difference was to be well marked.

The plaintiff contends that since decisions of this court and of the state courts of Texas, and for that matter courts of a majority of the states of the Union, hold organizations, such as the plaintiff, a partnership, that it may not be said to be a corporation, or, a joint stock company, or, an association.

Massachusetts National Bank vs. Wehrman, 202 U. S. 295;
Claggett vs. Kilbourne, 66 U. S. 340;
Crocker vs. Malley, 249 U. S. 223;
Elliott vs. Freeman, 220 U. S. 178;
In re Ballard, 279 F. 54;
Malley vs. Howard, 281 F. 363;
In re Trust, 222 F. 1012;
Chicago Title Trust Co. vs. Smietanka, 275 F. 60;
Malley vs. Bowditch, 259 F. 809;
In re Parker, 275 F. 868;
Roberts vs. Anderson, 226 F.
Industrial Lumber Co. vs. Texas Pine Land Assn. 72 S. W. 875;
McCamey vs. Hollister Oil Co. 241 S. W. 689;
Westside Oil Co. vs. McDorman, 244 S. W. 167;
Slaughter vs. American Baptist Publishing Society, 150 S. W. 224;
Fisheries Co. et al. vs. McCoy, 202 S. W. 343;
Wells vs. Mackey Telegraph Co., 239 S. W. 1001;
Hardee vs. Adams Oil Assn., 254 S. W. 602;
Willis vs. Greiner, 25 S. W. 858;
Burton vs. Grand Rapids, 31 S. W. 91;
Dee vs. Taylor, 227 S. W. 361;
Davis vs. Hudgins, 225 S. W. 73;
Morehead vs. Greenville, 243 S. W. 546;
Wrightington, 2nd Edition, on Unincorporated associations and business trusts.

[fol. 15] No debate can follow the assertion that the trustees of such association, and probably the members thereof, are liable for debts to third parties but when they are viewed from a taxing standpoint and in that herding where the accepted classification puts them as

well known and distrinctive commercial enterprises they wear, likewise, another label—another livery—another name.

The mere fact that the membership is such an association or joint stock company would be liable for a tort or for a debt, or that the ownership of the property might not seem to change, would not, of itself, divest such association or joint stock company of its standing as an association or joint stock company. In other words such aggregations of men have some points of similarity with partnerships; more points of similarity with partnerships than do corporations, and, yet, in one sense the corporation is also a partnership, even though it is always recognized as legally free from and independent thereof and stands and is to be treated as an artificial person. Nowhere in the articles of association is the plaintiff referred to as a partnership; this suit is not brought as a partnership; the owners of it do not appear here and sue in their individual capacities. They come here under section 6149 of the revised statutes of Texas which authorized an association or joint stock company to sue and be sued. An unincorporated company, fundamentally a large partnership, may be said to be an association, and with certain provisions may be said to be a joint stock company, and it will differ mainly from a partnership in that it is not bound by the acts of the individual partners, but only by those of its managers; that its shares are transferrable; and that it is not dissolved by the retirement, death bankruptcy, etc., of its individual members.

fol. 16] A joint stock company at common law was hybrid, midway between a corporation and a partnership, having some of the characteristics of each, but there was no delectus personæ. From lexicographers, and, decisions gathered therein, we may safely say that such associations are not pure partnerships, nor, are they pure corporations; not the first, because their members are recognized as an aggregate body; not the second, for their members are more or less able to contribute to the debts of the collective whole.

Mr. Justice Gray, in Karrick vs. Hannaman, 168 U. S. 334, defines partnership as follows:

"A contract of partnership is one by which two or more persons agree to carry on a business for their own benefit, each contributing property or services and having a unity of interest in the profits. It is, in effect, a contract of mutual agency, each partner acting as a principle in his own behalf, and as agent for his co-partners."

A partnership which did not have the characteristics of an association or of a joint stock company is merely a partnership. When it has such characteristics it becomes that whose character it has. As such it comes within the provisions of the law which relate *ot* it. A cow is no less a cow because it is black. An association and a joint stock company, are no less such association, or, joint stock company, because they may possess a similitude to a partnership. It is difficult to build an entity, so far as organization for carrying on the business of the world is concerned, without there being some similarity between such organizations, but general similarities do not

determine, either, the character, or, the name thereof, both being dependent upon the distinguishing characteristics for definition and classification.

In Haiker Sugar Co. vs. Johnstone, 249 F. 103, the circuit court for the ninth circuit in writing about this troublesome subject, said:

[fol. 17] "This is the pivotal point in the case, for in making distinction between joint stock associations and partnerships the congress must have had in mind that there are substantial points of difference between such relationships. It is notic-able that the arrangement under examination lacks the element of changability of partnership or transferability of shares, an element often used as a determ-ing criterion as between ordinary partnerships and joint stock companies. Bates on partnerships, 72, * * *. In a joint stock company the members have no right to decide what new members shall be admitted to the firm; on the other hand, the right of delectus personarum is an inherent quality of the ordinary partnership, * * * A joint stock company often consists of a large number of persons, between whom there is no special relationship or confidence; the retirement or death of a member words no dissolution; while a partnership though it may consist of several persons, generally is made up of a few, who are drawn to each other by feelings of mutual confidence, and no member is at liberty to retire and substitute another as a partner. In joint stock companies the business is generally managed by directors or other designated officers of the association, and the shareholder, as such, is without power to contract for the company; whereas, in a partnership any member may bind the partnership."

2nd

That this is the construction of the statute that has been given by an executive department of the government is also important. The courts give great weight to a construction placed upon an act of the Congress by the executive department which is charged with the duty of carrying it into effect.

Not a controlling weight, but strongly persuasive:

United States vs. Hermanos, 209 U. S. 337;
United States vs. Finnell, 185 U. S. 236;
United States vs. Alabama, 142 U. S. 615;
Pennoyer vs. McConnavghy, 140 U. S. 1;
Scholl vs. Fauche, 138 U. S. 562;
Robertson vs. Downey, 127 U. S. 506;
United States vs. Johnston, 124 U. S. 236;
United States vs. Hill, 120 U. S. 169;
Brown vs. U. S. 113 U. S. 568;
United States vs. Moore, 95 U. S. 760;
Swift vs. U. S., 105 U. S. 691.

[fol. 18] 3rd

The plaintiff contends that the Commissioner of Internal Revenue, in article 1501, of the regulations promulgated with reference to the act of 1918 attempted to legislate. Such regulation is as follows:

"The statute recognized three chief classes of persons, to-wit: Individuals, partnerships and corporations. Corporations include associations, joint stock companies, and insurance companies, but not partnerships properly so called."

It is contented that the phrase "property so called," limits and defines partnerships in a way that the Congress neither limited or defined.

While it has been settled that regulations made in pursuant of statutory authority have the force and effect of the law.

Maryland Casualty Co. vs. U. S. 251, U. S. 342;
United States vs. Eliason, 16th Pet. (U. S.) 291;
Ex parte Reed, 100 U. S. 13;
United States vs. Eaton, 144 U. S. 677;
Caha vs. U. S. 152 U. S. 211;
In re Kollock, 165 U. S. 526.

The Congress alone has the power to legislate, Constitution, article 1, section 1. It alone has the power to lay taxes, article 1, section 8. It may not delegate this power.

Morrill vs. Jones, 106 U. S. 466;
United States vs. United Verde Copper Co., 196 U. S. 207;
United States vs. Butter, 195 F. 657.

But when the Internal Revenue office explained in this regulation its understanding of the statute it was not legislating. It was enforcing.

[fol. 19] That the Congress, after this construction, passed a similar law with the exact working would certainly indicate that it was satisfied with the construction and definition that the executive department had placed on its act.

Fisk vs. Henarie, 142 U. S. 446.
Edwards vs. Wabash, 264 F. 610.

4th

It is contended that this construction given an unconstitutional tinge to the act. As, for instance, when such a tax is imposed upon a member by reason of an alleged income, and such individual member is in fact without a net income, the tax instead of being an income tax, within the sixteenth amendment, is a direct tax, which, under Article 1, section 2, clause 3, and, article 1, section 9, clause 4, of the constitution of the United States must be proportioned in accordance with the population of the several states.

The sixteenth amendment to the constitution provides:

"The Congress shall have power to levy and collect taxes on incomes from whatever source derived, without apportionment among the several states, and without regard to any sensus enumeration."

A graduated income tax is constitutional.

Brushaber vs. U. P. R. R., 240 U. S. 1;
Realty Co. vs. Anderson, 240 U. S. 115.

A person, in order to question the constitutionality of a statute, must show that the alleged unconstitutional feature injures him, and, in fact, deprives him of rights secured to him by the constitution. Rule vs. Johnson, 289 F. 964.

The stockholders of the plaintiff whose rights are said to be affected in this case, and for whom the plaintiff is solicitous in this suit, are not parties to this litigation and would not be bound by any determination reached herein. Therefore, the constitutional question raised by the amended bill and the very learned argument therein is not in the case. It might be observed, however, that a statute is not to be interpreted unconstitutional if such interpretation can be reasonably avoided.

[fol. 20] Insurance Co. vs. Kelly, 282 F. 772.

And the presumption is that a statute is constitutional.

Power Co. vs. Power Co., 283 F. 606;
Trade Co. vs. Lorillard, 283 F. 999;
United States vs. Cordin, 287 F. 565;
Railway Company vs. U. S. 287 F. 728.

In the case of Labelle Iron Works vs. U. S. 256 U. S. 377 the court said:

"The construction of the excess profits tax provisions as basing the tax on invested capital, which is determined only by the value of the assets at the time of their acquisition to the exclusion of subsequent increase of value, does not deprive the tax payer of due process of law, since equality of taxation can never be attained, and the tax in question applies equally to all corporations similarly situated."

The observation applies, likewise, to the tax imposed on joint stock associations because it applies equally to all such companies similarly situated, and is, therefore, uniform.

It follows from what has been said, that recovery by the plaintiff will be denied and judgment may be drawn for the defendant.

Wm. H. Atwell, United States District Judge.

[File endorsement omitted.]

[fol 21] IN UNITED STATES DISTRICT COURT

JUDGMENT—Filed March 3, 1924

On the 27th day of February, 1924, came on for trial the above entitled cause and appeared the parties plaintiff and defendant by their respective counsel and announced ready for trial, and it appearing to the court that the parties have entered into a stipulation and filed the same with the papers in the cause expressly waiving a trial by jury, and the matters of fact as well as of law being submitted to the

ourt, and the court being fully advised in the premises, is of the pinion the law is for the defendant and that plaintiff should take othing by its suit herein.

It is therefore on this, the 3rd day of March, 1924, the order and udgment of the court that the plaintiff Burk-Waggoner Oil Associaion, an unincorporated association, take nothing by its suit herein, nd that the defendant, George C. Hopkins, Collector of Internal Revenue, be and he is hereby judged to go hence without day and ecover all his costs incurred in this behalf.

It is the further order of the court that all such processes issue as hall be required to make the provisions of this judgment effective.

And to this judgment of the Court herein plaintiff by its attorneys bjects and excepts.

Wm. H. Atwell, Judge.

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fol. 22] IN UNITED STATES DISTRICT COURT

MOTION AND ORDER EXTENDING TIME—Filed March 20, 1924

Now comes the Plaintiff, Burk-Waggoner Oil Association, and hows to the Court that this term of Court adjourns on Saturday, Iarch 22nd, and that additional time is needed within which to preare and file Bill of Exceptions herein.

Wherefore, plaintiff prays for an extension of Thirty (30) days rom and after the adjournment within which to prepare, have llowed and file- said Bill of Exceptions.

Weeks, Morrow & Francis, Attorneys for Plaintiff.

fol. 23] On this, the 20th day of March, A. D. 1924, came the laintiff and made application for an order extending the time for gning, allowance and filing of the Bill of Exceptions herein; and ause being shown therefor such extension is granted and the time or signing, allowance and filing of Bill of Exceptions of the above amed Plaintiff is extended for 30 days from and after the last day f the present term of court, to-wit, from and after the 22nd day of Iarch, A. D. 1924.

Wm. H. Atwell, Judge.

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fol. 24] IN UNITED STATES DISTRICT COURT

Bill of Exceptions—Filed April 19th, 1924

CAPTION

Be it remembered that at a term of the District Court of the United tates in the Fifty Circuit thereof, and in and for the Northern Disict of Texas, on the 14th day of January, 1924, and which term djourned on the 22nd day of March, 1924, the Honorable William . Atwell, United States District Judge, presiding, the following

proceedings were had, and the following cause came on for trial and was tried, to-wit:

IN THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF TEXAS, DALLAS DIVISION

No. 3301. At Law

BURK-WAGGONER OIL ASSOCIATION

vs.

GEO. C. HOPKINS, Collector of Internal Revenue

STIPULATION RE AGREED STATEMENT OF FACTS

This cause came on for hearing before the Honorable William H Atwell; present Harry C. Weeks, Esq., and John M. Sternhagen, Esq. attorneys for the Plaintiff; N. A. Dodge, Esq., and Arthur H. Dei bert, Esq., attorneys for Defendant, and a jury being waived in writ ing, thereupon the following evidence, and that only, was submitte to the court.

The following stipulation of facts was duly executed, filed and sub mitted to the Court, to-wit:

[Title omitted]

[fol. 25] Stipulation

It is agreed by and between the Burk-Waggoner Oil Association plaintiff herein, and George C. Hopkins, Collector of Internal Rev enue, defendant herein, both parties acting by and through thei respective attorneys of record, that the following facts shall be take as true. This stipulation is made subject to the right of either party to introduce additional evidence at the trial of the above named cause

In pursuance of the above, it is agreed as follows:

The enterprise known as Burk-Waggoner Oil Association wa created by written agreement executed on the fifteenth day of No vember, A. D. 1918, by R. M. Waggoner, Clois L. Greene, Lee Cren shaw, D. H. Melton, W. H. Anchor, and A. H. Murchison.

This written agreement was styled Articles of Association, and wa filed for record in the Deed Records of Wichita County, Texas, on December 27th, 1918, and is recorded in Vol. 107, pages 579 to 582 Deed Records of Wichita County, Texas. The said Articles of Asso ciation are as follows:

"Burk-Waggoner Oil Association

Articles of Association

STATE OF TEXAS,
Wichita County:

Article I

Know all men by these presents: That we, R. M. Waggoner, Clois L. Greene, Lee Crenshaw, D. H. Milton, W. H. Anchor and A. H. Murchison do hereby form an unincorporated joint stock association to be known and styled Burk-Waggoner Oil Association (hereinafter referred to as the Company), which shall continue in existence during the lives of the said R. M. Waggoner, Clois L. Greene, Lee Crenshaw, D. H. Milton, W. H. Anchor and A. H. Murchison and for [fol. 26] twenty one years after the death of that one of said persons who last dies, unless sooner dissolved as herein provided.

The principal office of the Company shall be at Wichita Falls, Texas, and its business is to be carried on in the County of Wichita in the State of Texas, and at such other places in Texas, and elsewhere as the Board may determine.

Article II

The general purposes of this company are: The Manufacture of refined oil, gasoline, and all other products of crude petroleum, and market and sell, the same to purchase and acquire the crude oil necessary therefor, and to contract or otherwise acquire, operate and maintain all plants, refineries, structure, machinery, equipment, appliances and other things necessary to that end to engage in the general merchandise of petroleum and the manufactured products thereof, and such other articles as may be advantageously sold or handled in connection therewith to transport oil or any article manufactured therefrom, and to construct, operate and maintain all pipe or pipe lines and machinery necessary for that business to purchase, lease, contract, for own, hold and mine lands containing or supposed to contain oil, gas or other minerals, and to sell and market, or refine the same and generally to do either any or all of the things above named and anything properly incident thereto.

Article III

The capital stock of this company is sixty thousand dollars divided into 600 shares of one hundred dollars each, and shall be evidenced by certificates of interest of One Hundred Dollars, each to be issued as hereinafter provided.

Article IV

The certificates of stock shall be issued and signed by the Board of Trustees, and countersigned by the Secretary of said Board, and shall be in substantially the following form, to-wit:

[fol. 27] (Joint Stock Association Unincorporated)

Member's Certificate of Interest

This is to certify that —— —— is the owner of — fully paid shares of beneficial interest in the Burk-Waggoner Oil Association a joint stock association transferable only on the books of the company by the owners thereof in person, or by duly authorized attorney upon the surrender of this certificate properly endorsed.

This certificate of interest is subject to the provisions and covenants contained in the Article of association of the said Burk-Waggoner Oil Association dated the 15th day of November 1918 and any amendments thereto and the By-Laws of said Company present or future and the provisions hereof.

No member of said company or owner or holder of this certificate as such, shall have any authority, power or right whatsoever to do, or transact any business whatever for on behalf of or binding on the Company or any member thereof and no member of this company shall be personally liable for any debts covenants, demands, contracts of any kind or torts of this company beyond the payment in full of the price for which his share or shares were sold by him the company.

This certificate shall be the sole and only evidence of membership in said company.

Witness the signature of the officers of said company duly authorized.

Issued and signed this the — day of ——, A. D. 19—.

—— ——, President.

Attest: —— ——, Secretar-.

All the conditions and limitations stated in the above form shall be binding on each member (shareholder) his heirs, assigns and legal representatives, or any person holding certificates.

[fol. 28] Such certificates shall be transferrable only on the books of the company in accordance with the articles of association and by-laws. Shareholders whose certificates stand in their names on the books of the company shall alone or considered within the terms of this instrument, and shall alone be entitled to vote, receive dividends or receive notices as herein provided, or shall have the rights of owners. Any shareholder may at any time transfer or sell his share or any of them, but each holder of a share hereunder, or of a certificate thereof shall be held by the fact, of his acceptance of it to have assented to this trust, these articles of association and the By-laws of the company and to all instructions and acts performed in pursuance hereof.

In case of a loss or accidental destruction of a certificate of stock the trustees may cause to be issued a new certificate on such terms as they may see fit.

Article IV

Shareholders in this Company shall have no legal right to the trust property held from time to time by the Trustees herein provided for, and especially shall they have no right to call for any partition of the trust, property, or dissolution of the trust but the shares shall be personal property carrying the right of division of the profits, and at the termination of said trust by expiration of the period fixed for its existence or dissolution otherwise, the shareholders shall be entitled to a division of the principal and profits in due proportion to the number of shares held by each.

Article VI

The death, insolvency, or bankruptcy of a member of the company or the transfer of his interest by sale, gift, devise, descent, operation of law, or otherwise, during the life of the company, or trust shall not work a dissolution thereof or have any effect upon same, its operation or mode of business, nor shall it entitle his representatives, heirs or assigns, to an account or to take any action [fol. 29] in the courts in law or equity or otherwise against the company, its members, Trustees, officers or its property or assets or business operations which shall remain intact and undisturbed thereby but they shall simply and only succeed to the right of the original member to the certificate of membership and the shares it represents subject to these articles of association, the amendments thereto and the by-laws of the company now or hereafter adopted.

Article VII

The entire affairs of the company shall be managed by a Board of Trustees, consisting of six members each of whom shall own at least a certificate of membership in the company for not less than one share. The first board of trustees, which is hereby appointed, shall be composed of the following persons:

R. M. Waggoner, Clois L. Greene, Lee Crenshaw, D. H. Milton, W. H. Anchor and A. H. Murchison who shall continue in office until the first Tuesday in December, A. D. 1919 and until their successors are elected as herein provided for.

Each subsequent Board shall be elected by a majority of the shares present or represented, at a meeting of the shareholders to be held annually on the first Tuesday in December of each year, or as soon thereafter as practicable, beginning with the first Tuesday in December 1919 and shall continue in office for one year and until their successors shall have been elected.

Each Board shall elect its own President, such vice president as it may see proper to elect, Secretary and Treasurer and may create such other officers, filling them by appointment and prescribing the duties appertaining thereto, as they may deem wise, necessary or convenient to carry on the business of the company.

[fol. 30] The title to all property acquired to be acquired from time to time by the company and all investments shall be made and held in the names of the then Trustees as such, the survivor or survivors of them, under a declaration of trust for and on behalf of the Company such trustees shall hold said property as joint tenants and not as tenants in common, upon the trusts and with the powers herein stated. The trustees in their capacity as such, may sue and be sued in any court of law or equity or the company may sue or be sued in the company name as provided for by the Statutes of Texas.

The Trustees shall by a vote of a majority of the Board, have full power and authority to conduct the business and the affairs of the company to purchase, contract for, lease or otherwise acquire any property necessary or proper for the purposes of the company to sell and coneyv any part of the property of the company to make all necessary repairs, extensions and additions, to borrow money on the credit of the company and if deemed advisable, issue mortgage debentures therefor secured by a mortgage or deed of trust upon the property of the company executed upon such terms as they may deem proper and generally to do all things which in their judgment are necessary and prudent in the management and conduct of the company. Any debt incurred by the trustees shall be a charge on the property of the company in preference to the claim or claims of any shareholders as such; but the Trustee shall be and they are authorized in the conduct of the business, to sell in due course of business the goods, wares and merchandise of the company or other trust, property free of incumbrance whatsoever provided, of course, that any mortgaged property shall be sold only in conformity with the terms of the mortgage, or deed of trust given.

The Board of Trustees may fix and regulate their own time and place of meeting and a majority thereof shall constitute a quorum and possess and exercise all the powers of a full Board.

[fol. 31] Should any vacancy or vacancies in the Board occur from the death, resignation or removal of a member or members of the Board, or otherwise, the remaining members may fill the vacancy or vacancies, subject to the right of the shareholders to do so instead, should they see proper to exercise the right, the survivor or survivors of the Trustees, or in case of resignation the remaining Trustees shall have all the powers and rights and exercise all the functions of a full Board until the va-ncy or vacancies, are filled.

The Board of Trustees may select a manager or managers for all or any part of the Company's property or business, and may employ such agents, servants and employees, fixing their compensation and entrusting them with such authority and duties as they may deem wise, including the authority to buy and sell goods, wares, merchandise, material, supplies, machinery, appliances and other things necessary to its operation in due course of business.

The Board of Trustees may from time to time declare and pay such dividends from the earnings of the company as they deem expedient.

Article VIII

A Declaration of trust in accord herewith shall be executed by the Trustees appointed hereunder binding alike on them, the survivor or survivors of them, their successors and the survivor or survivors of them, and all persons dealing with them. The Trustees, the survivor, or survivors of them, their successors, and their survivor or survivors, shall have no power to bind the shareholders or members personally and in every written contract they shall enter into relating to the business of this company its property or any part thereof reference shall be made to said declaration of trust, and the person, firm or corporation so contracting with them shall look [fol. 32] only to the funds and property legal and equitable of the company under said contract for the payment of any debt, damage, judgment or decree or of any money that may become due and payable in any way by reason thereof and neither any of the Trustees, nor the shareholders, present or future, shall be personally liable therefor or for any debt, incurred or engagement or contract made by the Board of Trustees, or any officer, agent or servant acting under them on behalf of the company.

Furthermore, the funds and property of the company of every character shall stand primarily charged with the burden of paying any claim or money demand established or existing on account of the operations and business of the company whether founded on contract or tort to the end that the members of the company may be protected from personal liability on account thereof.

In all deeds and conveyance to said trustees or any of them, or to their successors, or any of them it shall be set forth that such grant, conveyance or transfer is to him or them as Trustees of the Burk-Waggoner Oil Association to be held subject to the declaration of trust made pursuant to the Articles of Association, and the By-Laws of the Company present or future.

Article IX

The Board of Trustees appointed hereby may adopt such By-Laws in harmony herewith as they thing proper. The Declaration of Trust required hereunder, and such By-Laws as they may adopt, shall be signed and acknowledged by the Trustees, in the manner required by the laws of Texas for the registration of conveyances of real estate, to the end that the same may be recorded if it be deemed necessary or expedient.

Article X

At any annual meeting of the shareholders or any special meeting called for that purpose, the Articles of Association may be amended [fol. 33] by a vote of three-fourths of the shares present or represented, and By-Laws may be adopted, repealed, or amended in any respect not inconsistent with the Articles of Association by a vote of two-thirds of the shares present or represented.

A majority of the shares then issued and outstanding at any meeting of the share holders whether annual or special shall be necessary to constitute a quorum to transact business.

Article XI

The share or certificate holders shall meet annually on the first Tuesday of June of each year at the principal office of the Company without further notice to consider the affairs of the Company and transact such business as may be inaugurated by them, or as may be submitted for their consideration by the Board of Trustees. Should they fail to meet on said date, they shall have their annual meeting as early thereafter as practicable and to that end the Board of Trustees shall issue to the shareholders ten days notice to be given as provided by Article XII below in the case of special meeting calling an annual meeting at a date named. At each meeting of the share or certificate holders, each member present or represented by a duly accredited agent or attorney, shall be entitled to cast as ma-y votes upon any proposition as he may have shares or membership interest provided he shall vote only such as has stood in his name on the books of the Company for ten days prior to the election.

Article XII

The Board of Trustees shall whenever they think it necessary call a special meeting of the shareholders, stating the purpose thereof, upon notice to that effect deposited in the post office at the place of the principal offices of the Company addressed to each shareholder at his registered post office address ten days before the date of the proposed meeting.

It shall be the duty of the trustees to call a special meeting of the shareholders when requested to do so by the holders of one fourth of the shares then issued and outstanding. In case the Trustees [fol. 34] shall fail or refuse to do so, the owners of one-fourth of the shares of the Company may themselves call a meeting signing a written notice to that effect, stating the purpose of the meeting, such notice to be given for the time and in the manner above stated.

Article XIII

The President, or in his absence, a Vice President, shall sign all certificates of membership, preside at all meetings of the Board of Trustees and of the shareholders, and shall do and perform and render such acts and services as the Board of Trustees shall prescribe and require, and shall receive such compensation for services as may from time to time be fixed by the Board.

The Secretary or Assistant Secretary shall countersign all certificates of membership and shall keep such minutes, records and books as the Board of Trustees may require, attend all meetings of the Board of Trustees, and render such services as may be imposed upon him. The Treasurer shall perform such duties as the Board of

Trustees may impose upon him. The offices of Secretary and Treasurer may be filled by one person if the Board sees fit.

Article XIV

The members of the Board of Trustees shall at all times be subject to the orders of the shareholders, who may at any time and for any cause by a vote of a majority of all the shares then issued and outstanding remove any one or all of them from office and appoint and devolve upon other members the duties and functions of the office.

All conveyances of real estate shall be made by a majority of the Trustees as such under such authority of a resolution of the Board or the President or Vice-President of the Company under like authority. Upon any change in the membership of the Board of Trustees being made all members of the Board as it may exist after the change is made shall execute and acknowledge an instrument certifying the members of the Board and the changes made and each [fol. 35] new Trustee shall qualify before entering upon the discharge of his duties as such, by signing and acknowledging a written acceptance of the trust and a declaration that he will execute the same subject to and in accordance with the Articles of Association the Declaration of Trust and the By-Laws of the Company present and future.

The Trustees or a majority of them, and the Secretary shall from time to time as the Articles or By-Laws are amended certify under the seal of the company to the same as amended to the date of the certificate and their certificate to that effect shall constitute full proof of the facts thereby shown.

Article XV

No trustee shall be liable for the fraud, error or negligence of a co-trustee to which he has not been a party. Any trustee may relieve himself of any responsibility to the shareholders for any acts of the Board of Trustees of which he does not approve by causing his disapproval to be noted by the Secretary upon records of the Trustees.

Article XVI

Forty Thousand ($40,000.00) Dollars of the capital stock of this company as organized shall be paid by the conveyance to the Trustees above named to the following described oil and gas lease, to-wit: Being the sixty (60) acres in the form of a square in the Northeast Corner of Block 84 Red River Valley Land in Wichita County, Texas, being a part of the land covered by lease from R. M. Waggoner, to C. F. Wilson, Henry Evans, O. P. Darsey, L. P. Crenshaw, A. P. Howard, E. H. Pigg, R. M. Waggoner, Clois L. Greene, Lee Crenshaw, W. H. Anchor and A. H. Murchison, dated September 11th, 1918, and recorded in the Deed Records of Wichita County, Texas, reference to which is here made, the balance of the

capital stock to be paid for in cash which said oil and gas leases are here referred to for a particular description of the premises and conditions thereof, and the Association shall accept said oil and gas lease subject to all of the terms and conditions therein contained. There shall be issued, when said oil and gas leases are [fol. 36] conveyed to the Trustees hereinabove named, the said Forty Thousand Dollars of stock in payment for said oil and gas leases, it being agreed between the parties hereto that said oil and gas leases are reasonably worth the said sum of Forty Thousand Dollars.

The stock of the association may be increased at any time by a vote of a majority of all of the stock present and represented at a meeting of the stockholders called for that purpose.

Article XVII

A dissolution of the company by the shareholders may be effected by a vote of three-fourths of all the membership certificates or shares then issued and outstanding, but the shareholders shall not dissolve this Company at any time prior to the period fixed herein for its final dissolution while there is outstanding against the property of the company the bonds or obligations of the Trustees, as such, secured by a mortgage on the property of the company without the written consent of the holders of two-thirds of said bonds and any dissolution shall be made without prejudice to any debts or claims against the company contracted by the Trustees.

In testimony whereof, witness our official signatures this the 15th day of November, A. D. 1918.

R. M. Waggoner, Clois L. Greene, A. H. Murchison, Trustees Burk-Waggoner Oil Association. Lee Crenshaw, W. H. Anchor, D. H. Milton.

THE STATE OF TEXAS,
County of Wichita:

Before me the undersigned, a Notary Public in and for Wichita County, Texas, on this day personally appeared D. H. Milton, R. M. Waggoner, W. H. Anchor, Lee Crenshaw and Clois L. Greene, Trustee of Burk-Waggoner Oil Association, known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they executed the same for the purposes and consideration therein expressed and in the capacity therein stated.

[fol. 37] Given under my hand and seal of office this the 26th day of December, A. D. 1918. A. L. Huey, Notary Public, Wichita County, Texas. (Seal.)

THE STATE OF TEXAS,
County of Wichita:

Before me the undersigned, a Notary Public in and for Wichita County, Texas, on this day personally appeared D. H. Milton, R. M. Waggoner, W. H. Anchor, Lee Crenshaw and Clois L. Greene,

Trustees of Burk-Waggoner Oil Association, known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they executed the same for the purposes and consideration therein expressed and in the capacity therein stated.

Given under my hand and seal of office this the 26th day of December, A. D. 1918. A. L. Huey, Notary Public, Wichita County, Texas. (Seal.)

THE STATE OF TEXAS,
County of Wichita:

Before me, the undersigned authority, on this day personally appeared A. H. Murchison known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this 16th day of December, A. D. 1918. C. V. King, Notary Public in and for Wilbarger County, Texas. (Seal.)

THE STATE OF TEXAS,
County of Wichita:

Know all men by these presents: That we, R. M. Waggoner, Clois L. Greene, Lee Crenshaw, D. H. Milton, W. H. Anchor and A. H. Murchison, Trustees for Burk-Waggoner Oil Association, a joint stock association for ourselves, and our successors under said trust, [fol. 38] declare that we and they hold all of the property, real and personal or of any species conveyed and granted and in any way coming to us or them as Trustees of Burk-Waggoner Oil Association subject to the articles of association and by laws now or hereafter adopted by said company and upon the trusts and conditions and subject to all of the stipulations and provisions of said articles of association.

Witness our hands this 15th day of November, A. D. 1918.

R. M. Waggoner, Clois L. Greene, A. H. Murchison, Trustees Burk-Waggoner Oil Association. Lee Crenshaw, W. H. Anchor, D. H. Milton.

THE STATE OF TEXAS,
County of Wichita:

Before me the undersigned authority on this day personally appeared Clois L. Greene, Lee Crenshaw, D. H. Milton, W. H. Anchor and R. M. Waggoner, Trustees of the Burk-Waggoner Oil Association and known to me to be the persons whose names are subscribed to the foregoing instruments and acknowledged to me that they executed the same for the purposes and consideration therein expressed and in the capacity therein stated.

Given under my hand and seal of office this the 26th day of Dec., A. D. 1918. A. L. Huey, Notary Public, Wichita County, Texas. (Seal.)

THE STATE OF TEXAS,
County of Wilbarger:

Before me, the undersigned authority on this day personally appeared A. H. Murchison known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

C. V. King, Notary Public in and for Wilbarger County, Texas.

Filed for record Dec. 27, 1918, at 3:21 P. M.
Recorded January 3, 1919, at 4:40 P. M.
W. T. Harris, Clerk County Court, Wichita County, Texas, by —— ——, Deputy.

[fol. 39] STATE OF TEXAS,
County of Wichita:

I, W. T. Harris, Clerk of the State and County aforesaid do hereby certify that the above and foregoing instrument of writing is a true and correct copy of an Article of Association given by Burk-Waggoner Oil Association dated 15th day of November as the same appears of record in the Deed Records of Wichita County, Texas, in Vol. 107, pages 579-80-81-82.

Given under hand and seal of office at office in Wichita Falls, Texas, this 30 day of Jan. A. D. 1919.
W. T. Harris, County Clerk, Wichita County, Texas."

Said instrument provided for a capital stock for said enterprise of $60,000.00, divided into six hundred shares of par value of $100.00 each, and the form of certificate or receipt to be issued therefor was provided for in Article 4 thereof. Said capital stock was subscribed and paid for by those forming the association and by others who were solicited to join. Part of said capital stock was paid for in cash, the remainder being paid for by transferring to the Trustees of the enterprise the oil and gas lease hereafter referred to.

To every subscriber certificates of stock in the form provided for in Article 4 were issued and these certificates were considered by all concerned transferable, and were transferred freely, and the person in whose name certificates stood upon the records of the enterprise was considered and deemed by all concerned to be the holder of the interest specified therein.

This enterprise acquired the oil and gas lease upon the Northeast sixty (60) acres in the form of a square out of block No. 84, Red River Valley Lands Subdivision, in Wichita County, Texas, on December 14, 1918. The conveyance is as follows:

[fol. 40] STATE OF TEXAS,
County of Wichita:

Know all men by these presents: that we, C. F. Wilson, Henry Evans, D. H. Milton, O. P. Darsey, Clois L. Greene, W. H. Anchor, E. H. Pigg, L. P. Crenshaw, A. P. Howard, R. M. Waggoner, Lee Crenshaw and A. H. Murchison for and in consideration of the sum of $1,000.00 and other good and valuable consideration cash in hand paid by R. M. Waggoner, Clois L. Green, Lee Crenshaw, W. H. Anchor, and A. H. Murchison, Trustees for the Burk-Waggoner Oil Association, a joint stock association, the receipt of which is hereby acknowledged and confessed, have granted, sold, conveyed and assigned and by these presents do grant, sell, convey and assign unto the said R. M. Waggoner, Clois L. Greene, Lee Crenshaw, W. H. Anchor and A. H. Murchison, Trustees all our rights, title and interest in and to that certain lease and leasehold estate covering 60 acres of land in the form of a square in the Northeast corner of said Block 84 being a part of the lands covered by lease of R. M. Waggoner and wife to the grantors herein dated September 6, A. D. 1918, and recorded in Volume 109, page- 26-27 of the Deed Records of Wichita County, Texas, reference to which is here made for full particulars.

To have and to hold unto the said R. M. Waggoner, Clois L. Greene, Lee Crenshaw, W. H. Anchor, and A. H. Murchison, Trustees and their successors and assigns forever, subject to the terms, conditions and stipulations of the original lease contract above referred to which terms and conditions and stipulations are assumed by the Grantees herein.

Witness our hands on this 14th day of December, A. D. 1918.
Lee Crenshaw, W. H. Anchor, D. H. Milton, Clois L. Greene, A. H. Murchison, E. H. Pigg, A. P. Howard, M. D., C. F. Wilson, R. M. Waggoner, L. P. Crenshaw, O. P. Darsey, Henry Evans.

Acknowledgments

STATE OF TEXAS,
County of Wichita:

Before me, the undersigned a Notary Public, in and for Wichita County, State of Texas, on this day personally appeared D. H. Milton, W. H. Anchor, L. P. Crenshaw, R. M. Waggoner and Lee Cren- [fol. 41] shaw, known to me to be the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that they executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 17th day of December, A. D. 1918. A. L. Huey, Notary Public, Wich- County, Tex. (Seal.)

STATE OF TEXAS,
County of Wilbarger:

Before me, the undersigned, a Notary Public in and for the County and State aforesaid on this day personally appeared A. H. Murchison, Clois L. Greene, E. H. Pigg, and A. P. Howard, known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged to me that they executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 16th day of December, A. D. 1918. C. V. King, Notary Public, Wilbarger County, Texas. (Seal.)

STATE OF TEXAS,
County of Wichita:

Before me, the undersigned authority, in and for Wichita County, Texas, on this day personally appeared C. F. Wilson, known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 17th day of December, A. D. 1918. Dave Throne, J. P. and ex Officio Notary Public, Wichita County, Texas. (Seal.)

[fol. 42] STATE OF TEXAS,
County of Floyd:

Before me, Kenneth Bain, a Notary Public in and for said County and State on this day personally appeared O. P. Darsey known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this 19th day of December, 1918. Kenneth Bain, Notary Public. (Seal.)

STATE OF TEXAS,
County of Eastland:

Before me, Connie Davis, a Notary Public in and for Eastland County, Texas, on this day personally appeared Henry Evans known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this 21st day of December, A. D. 1918. Connie Davis, Notary Public, Eastland County, Texas. (Seal.)

Filed for record December 28th, 1918 at 3:19 P. M.
Recorded January 1st, 1919, at 8:55 A. M.
W. T. Harris, Clerk County Court, Wichita County, Texas,
By —— ——, Deputy."

From the funds obtained from subscribers to said capital stock and upon the credit of individual members thereof, those in charge of the enterprise, to-wit, the Trustees appointed in said Articles of Association, were able to and did drill a well for oil and gas upon said property, which was completed on or about April 25, 1919, [fol. 43] as a very productive oil well. This caused a large enhancement in the value of said property and same was sold about May 5, 1919, for $2,000,000.00, since which time no business has been transacted by the enterprise except that incidental to winding up its affairs.

The operations so conducted resulted in a net profit of $1,838,053.90, all of which was received in the year 1919.

Those managing this enterprise learned from the published regulations and notices of the Bureau of Internal Revenue that the Bureau of Internal Revenue considered an enterprise like Burk-Waggoner Oil Association taxable as a corporation under the Revenue Act of 1918, and held that it was required by said regulations to file a return, and this was done on March 15, 1920. This return and report showed a tax liability of $552,602.02, which was paid as follows:

On March 15, June 12, and September 12, 1920, $138,150.51 upon each date; and on March 28, 1922, $145,827.67. A claim for abatement had been filed about December 15, 1920, seeding the abatement of the last quarterly payment due December 15, 1919. This claim was rejected, and a demand made for the amount of same plus interest, which was complied with under protest and duress on March 28, 1922. The interest on this payment accounts for the variance between it and the other payments. This last payment was paid to the defendant, Geo. C. Hopkins, as Collector of Internal Revenue for the Second District of Texas.

Two claims for the refunding of said taxes were filed by plaintiff, copies of same being attached hereto and marked "Exhibits "A" and "B". These claims were filed upon the tenth day of December, 1920, and the twenty-fourth day of April, 1922, respectively and the last claim has never been acted upon. The first claim was rejected.

[fol. 44] There are also attached copies of the original and amended returns made by Burk-Waggoner Oil Association, marked Exhibits "C" and "D".

A copy of the receipt given for the last payment made is attached hereto and marked Exhibit "E".

At the time the original return was made and at the time all the various payments were made, there were in force and effect regulations duly adopted and promulgated by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, requiring all organizations or enterprises similar to Burk-Waggoner

Oil Association to make returns substantially in accordance with that made by said association and to pay the tax shown to be due, and substantial penalties would have been asserted against Burk-Waggoner Oil Association had it failed to make said reports or pay such tax.

The payment of $145,827.67 made by plaintiff to defendant on March 28, 1922, was not made until plaintiff had received a letter from defendant dated March 22, 1922, stating that a warrant of distraint had been issued and would be levied upon its property if the tax was not paid. A copy of this letter is attached hereto and marked Exhibit "F". The said payment was made to avoid this seizure and sale and the imposition of further penalties.

There are also attached hereto a copy of a letter dated November 26, 1921, addressed to the plaintiff by the Commissioner of Internal Revenue, and a copy of a letter addressed to the Commissioner of Internal Revenue on March 5, 1920, by McAdoo, Cotton & Franklin and Weeks, Morrow, Weeks & Francis, attorneys for the plaintiff, marked Exhibits "G" and "H", respectively.

There is hereto attached as Exhibit "I" copy of a letter dated April 21, 1922, from plaintiff's attorney to the Collector of Internal Revenue at Dallas, Texas, forwarding a claim for refund of the sum of $409,774.03, together with copy of a reply from the said Collector of Internal Revenue, dated April 25, 1922, marked Exhibit "J", acknowledging receipt of the said claim, and stating that it would be forwarded to the Commissioner of Internal Revenue for final disposition.

[fol. 45] All exhibits attached are hereby made parts of this statement to the extent that said exhibits show what was done and how and when same was done, but the plaintiff does not agree that the filing of said returns or any of said claims or the making of said payments was an admission or agreement that it was taxable as a corporation under the Revenue Act of 1918, the effect of the said actions being considered a question of law for decision by the court.

A jury is expressly waived and it is agreed all matters of fact, as well as of law, shall be determined by the Court.

Weeks, Morrow & Francis, J. M. Sternhagen, Attorneys for Burk-Waggoner Oil Association, Plaintiff. Henry Zweifel, U. S. Atty., and N. A. Dodge, Spl. Asst., and A. H. Diebert, Spl. Atty., Attorneys for Geo. C. Hopkins, Collector of Internal Revenue, Defendant."

(Here follows Exhibit "A," marked side folio pages 46 and 46½)

[fol. 47] Claimant made original return of 1919 income and excess-profits tax in accordance with existing regulations, showing total net income of $1,838,053.90 and total tax liability of $552,602.02, upon which it has paid to date $414,451.53.

Of the above amount of "net income" (so called) $24,564.96 was derived from claimant's business of producing oil. The remainder was derived from the sale of capital assets. The tax upon the first amount, not considering the gain derived from the sale of capital

TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
Form 843—Jan., 1922
Comptroller General U. S.
January 18, 1922

EXHIBIT "A"

CLAIM FOR

- ☐ ABATEMENT OF TAX ASSESSED
- ☐ CREDIT AGAINST OUTSTANDING ASSESSMENTS
- ☐ REFUND OF TAXES ILLEGALLY COLLECTED
- ☐ REFUND OF AMOUNTS PAID FOR STAMPS USED IN ERROR OR EXCESS

IMPORTANT
File with Collector of Internal Revenue where assessment was made. Not acceptable unless completely filled in.

COLLECTOR'S NOTATION
District
Account number
Date received
Stamp here
Collector of Internal Revenue

State of Texas } ss:
County of Wichita }

NOTICE TO COLLECTOR
Collector must indicate in block above the kind of claim, except in Income Tax cases.

Date received by Administrative Unit
Stamp here

Burk-Waggoner Oil Association
(Name of taxpayer or purchaser of stamps.)

TYPE OR PRINT

Richita Falls, Texas
(Residence—give street and number as well as city or town and State.)

(Business address.)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below with reference to said statement are true and complete:

PERIOD	YEAR
From:	19
To:	19

1. Business in which engaged Producing oil
2. Character of assessment or tax 1919 Income & Excess-profit tax
(State for or upon what the tax was assessed or the stamps affixed.)
3. Amount of assessment or stamps purchased $552,602.02
4. Reduction of Tax Liability requested (Income and Profits Tax) $
5. Amount to be abated $
6. Amount to be refunded (or such greater amount as is legally refundable) $407,491.66
7. Dates of payment (see Collector's receipts or indorsements of canceled checks) 138,150.51 4-26-20 138,150.51
(If statement covers income tax liability, items 8-11, inclusive, must be answered.) 8-14-20 138,150.51
8. District in which return (if any) was filed 9-16-20
9. District in which unpaid assessment appears
10. Amount of overpayment claimed as credit $
11. Unpaid assessment against which credit is asked; period from to $

Deponent verily believes that this application should be allowed for the following reasons:

SEE STATEMENT ATTACHED

(Attach additional sheets if necessary.)

Sworn to and subscribed before me this 9th day of December, 1920

Harry C. Weeks Notary Public
Wichita County Texas
(Title.)

Signed:
R.M.Waggoner, President
Waggoner Bldg., Wichita Falls, Texas

46

(This affidavit may be sworn to before a Deputy Collector of Internal Revenue or Revenue Agent without charge.)

c2—11704

CERTIFICATES

Schedule No. _____

I certify that an examination of the records of the Bureau of Internal Revenue shows the following facts as to the assessment and payment of the tax:

NAME OF TAXPAYER.	Character of assessment and period covered.	List.	Year.	Month.	Page.	Line.	Amount.	Date paid.	District in which paid.
							$		

_____

Collector of Internal Revenue.

_____

Assessment Clerk, Commissioner's Office.

Claim No. _____

I certify that the records of my office show the following facts as to the purchase of stamps:

TO WHOM SOLD OR ISSUED.	Kind.	Number.	Denomination.	Date of sale or issue.	Amount.	If special tax stamp, state:	
						Serial number.	Period commencing—
					$		

_____

Collector _____ *District* _____

Claim No. _____

Schedule Number _____ District _____

Allowed or Rejected Number _____

_____
(Nature of tax.)

Claimant _____

Address _____

Examined and submitted for action _____, 19____

Schedule No. _____

Claim examined by—
Claim approved by—
Chief of Division.

COMMITTEE ON CLAIMS

Amount claimed... $_____ _____

Amount allowed... $_____ _____

Amount rejected... $_____ _____

o2—11704

GOVERNMENT PRINTING OFFICE

TREASURY DEPARTMENT
INTERNAL REVENUE SERVICE
Form 843—Jan., 1922
Comptroller General U.
January 18, 1922

EXHIBIT "B"

CLAIM FOR

- ☐ ABATEMENT OF TAX ASSESSED
- ☐ CREDIT AGAINST OUTSTANDING ASSESSMENTS
- ☐ REFUND OF TAXES ILLEGALLY COLLECTED
- ☐ REFUND OF AMOUNTS PAID FOR STAMPS USED IN ERROR OR EXCESS

IMPORTANT
File with Collector of Internal Revenue where assessment was made. Not acceptable unless completely filled in.

COLLECTOR'S NOTATION
District
Account number
Date received
Stamp here
Collector of Internal Revenue

State of Texas } ss:
County of Wichita }

NOTICE TO COLLECTOR
Collector must indicate in block above the kind of claim, except in Income Tax cases.

Date received by Administrative Unit
Stamp here

Burk-Waggoner Oil Association
(Name of taxpayer or purchaser of stamps.)

TYPE OR PRINT

(Residence—give street and number as well as city or town and State.)

Waggoner Building, Wichita Falls, Texas
(Business address.)

This deponent, being duly sworn according to law, deposes and says that this statement is made on behalf of the taxpayer named, and that the facts given below with reference to said statement are true and complete:

PERIOD	YEAR
From: Jan 1	19 19
To: Dec 31	19 19

1. Business in which engaged: Producing Oil
2. Character of assessment or tax: Income and Excess-profits tax (State for or upon what the tax was assessed or the stamps affixed.)
3. Amount of assessment or stamps purchased: $552,408.02
4. Reduction of Tax Liability requested (Income and Profits Tax): $409,774.03
5. Amount to be abated: $none
6. Amount to be refunded (or such greater amount as is legally refundable): $409,774.03
7. Dates of payment (see Collector's receipts or indorsements of canceled checks) 3/15/20 $138,150.51- 6/12/20 $138,150.51-9/12/20 (If statement covers income tax liability, items 8-11, inclusive, must be answered.)
8. District in which return (if any) was filed: Austin, Texas ($138,150.51-3/18/22 $145,827.67
9. District in which unpaid assessment appears: First 2 payments Austin, Tex. last 2 payments Dallas, Texas
10. Amount of overpayment claimed as credit: $
11. Unpaid assessment against which credit is asked; period from ____ to ____: $

Deponent verily believes that this application should be allowed for the following reasons:

See statement attached

(Attach additional sheets if necessary.)

Sworn to and subscribed before me this ____ day of ____, 19____

Signed:

(Title.)

(This affidavit may be sworn to before a Deputy Collector of Internal Revenue or Revenue Agent without charge.)

c2—11704

50½

CERTIFICATES

Schedule No. _____

I certify that an examination of the records of the Bureau of Internal Revenue shows the following facts as to the assessment and payment of the tax:

NAME OF TAXPAYER.	Character of assessment and period covered.	List.	Year.	Month.	Page.	Line.	Amount.	Date paid.	District in which paid.
							$		

_____
Collector of Internal Revenue.

_____
Assessment Clerk, Commissioner's Office.

Claim No. _____

I certify that the records of my office show the following facts as to the purchase of stamps:

TO WHOM SOLD OR ISSUED.	Kind.	Number.	Denomination.	Date of sale or issue.	Amount.	If special tax stamp, state:	
						Serial number.	Period commencing—
					$		

Claim No. _____

_____

Collector _____ *District* _____

Schedule Number _____ District _____

Allowed or Rejected Number _____

_____
(Nature of tax.)

Claimant _____

Address _____

Examined and submitted for action _____, 19____

Schedule No. _____

Claim examined by—
Claim approved by—
Chief of Division.

COMMITTEE ON CLAIMS

Amount claimed— $_____ _____

Amount allowed— $_____ _____

Amount rejected— $_____ _____

GOVERNMENT PRINTING OFFICE

c2—11704

assets, is $6,959.88. Claimant presents herewith corrected return in which the so called "income" derived from sale of capital assets is excluded and the tax calculated upon the remainder, also claim for refund of $407,491.65, the difference between tax paid to date and tax shown to be due by said corrected report, and claim for abatement for the unpaid portion.

Claimant, Burk-Waggoner Oil Association, is an unincorporated joint stock association, organized with a capital stock of $60,000.00 on November 15, 1918. Of this, $40,000.00 in par value was issued for an oil and gas lease on 60 acres of land in the N. E. corner of Block 84, Red River Valley Lands Subdivision in Wichita County, Texas. The remainder was sold and the funds used to drill an oil and gas well on said lease. The first well was highly productive. It was completed about April 21st, 1919, and on or about May 5, [fol. 48] 1919, all of the company's property, which consisted of said lease, the well and equipment, etc., on same was sold for $2,000,000.00, and it is from this transaction that the so called "income of $1,813,488.94 from the sale of capital assets was derived.

The Burk-Waggoner Oil Association never at any time engaged in any business other than developing and producing oil. It never owned any lease other than the one above described. It never bought and sold oil property or stocks. It was organized primarily to develop said 60 acre lease for oil, and conducted no other business.

It is claimant's contention,

1st. That the gain or enhancement in value of the capital assets of claimant, realized by the sale above referred to, is not income within the purview of the 16th Amendment.

2nd. That the distinction made in Gray vs. Darlington, 15 Wallace 45, between "income" and the enhancement in value of capital assets is controlling in arriving at what is included in "income" as used in said Amendment.

3rd. That the tax sought to be imposed is a direct tax.

4th. That, being a direct tax, and not being apportioned among the State, as the constitution provides, and not being upon income, and thus relieved from the necessity of apportionment by the 16th [fol. 49] Amendment, the attempt of the present income and excess-profits tax law to tax the gain and enhancement in value of capital, realized by a sale, is unconstitutional and illegal.

5th. That the present income and excess-profits tax law, as applied to claimant, is illegal and unconstitutional for numerous other reasons.

6th. That, for these reasons claimant's claims for refund and abatement should be sustained.

Reference is here respectfully made to the original and corrected returns of claimant for full data as to its organization, property, etc.

(Here follows Exhibit "B", marked side folio pages 50 and 50½)

assets, is $6,959.88. Claimant presents herewith corrected return in which the so called "income" derived from sale of capital assets is excluded and the tax calculated upon the remainder, also claim for refund of $407,491.65, the difference between tax paid to date and *tax shown to be due by said corrected report*, and claim for abatement for the unpaid portion.

Claimant, Burk-Waggoner Oil Association, is an unincorporated joint stock association, organized with a capital stock of $60,000.00 on November 15, 1918. Of this, $40,000.00 in par value was issued for an oil and gas lease on 60 acres of land in the N. E. corner of Block 84, Red River Valley Lands Subdivision in Wichita County, Texas. The remainder was sold and the funds used to drill an oil and gas well on said lease. The first well was highly productive. It was completed about April 21st, 1919, and on or about May 5, [fol. 48] 1919, all of the company's property, which consisted of said lease, the well and equipment, etc., on same was sold for $2,000,000.00, and it is from this transaction that the so called "income of $1,813,488.94 from the sale of capital assets was derived.

The Burk-Waggoner Oil Association never at any time engaged in any business other than developing and producing oil. It never owned any lease other than the one above described. It never bought and sold oil property or stocks. It was organized primarily to develop said 60 acre lease for oil, and conducted no other business.

It is claimant's contention,

1st. That the gain or enhancement in value of the capital assets of claimant, realized by the sale above referred to, is not income within the purview of the 16th Amendment.

2nd. That the distinction made in Gray vs. Darlington, 15 Wallace 45, between "income" and the enhancement in value of capital assets is controlling in arriving at what is included in "income" as used in said Amendment.

3rd. That the tax sought to be imposed is a direct tax.

4th. That, being a direct tax, and not being apportioned among the State, as the constitution provides, and not being upon income, and thus relieved from the necessity of apportionment by the 16th [fol. 49] Amendment, the attempt of the present income and excess-profits tax law to tax the gain and enhancement in value of capital, realized by a sale, is unconstitutional and illegal.

5th. That the present income and excess-profits tax law, as applied to claimant, is illegal and unconstitutional for numerous other reasons.

6th. That, for these reasons claimant's claims for refund and abatement should be sustained.

Reference is here respectfully made to the original and corrected returns of claimant for full data as to its organization, property, etc.

(Here follows Exhibit "B", marked side folio pages 50 and 50½)

[fol. 51] The Burk-Waggoner Oil Association made due return of its 1919 income and this return showed a total net income of $1,838,053.90 and a total tax liability of $552,402.02, all of which has been paid under protest as the dates above shown.

The Burk-Waggoner Oil Association has heretofore filed a Claim for Refund in the sum of $407,491.65 and a Claim for Abatement in the sum of $138,150.49, both of which claims have been rejected. Said company here and now renews these claims for the reasons set forth in same, and in addition thereto says that this claim should be allowed for the following reasons.

The Burk-Waggoner Oil Association made at the time its original return was filed an application for special assessment under the terms of Sections 327 and 328 of the 1918 Law, it being the contention that if the tax be determined without the benefit of said Sections, that, owing to abnormal conditions affecting the capital or income of the Burk-Waggoner Oil Association, it would suffer exceptional hardship, as is evidenced by the gross disproportion between the tax paid and the tax paid by representative corporations engaged in the same line of business.

This application for special assessment has been denied. The Burk-Waggoner Oil Association understands that the application was [fol. 52] refused because the Special Assessment Section used as comparatives only oil companies who had made sales of all of their holdings in the year 1919.

It is submitted that this method of comparison is incorrect. The Burk-Waggoner Oil Association was not engaged in the business of selling oil properties, nor does it seem possible that any corporation or association could be engaged in the business of selling all of its properties or liquidating. The business engaged in was producing oil. The fact that it sold all of its properties and liquidated in the year 1919 is the abnormal condition affecting its income, which is the basis of the right to special assessment.

This company contends that it should be compared to representative corporations engaged in the business of producing oil; that it should not be compared only with those which were highly successful. That the term "representative corporation" means substantially average corporations and that the average of a large number of corporations engaged in the oil business, including the very successful, the unsuccessful and those between, should be used as a basis of comparison.

Burk-Waggoner Oil Association also contends that the average small oil company for the year 1919 made no money whatsoever. That by far the greater per cent of those operating in the year 1919 are now insolvent. That this applies particularly to the locality [fol. 53] in which Burk-Waggoner Oil Association operated, and it is thought by the Burk-Waggoner Oil Association that the average corporation engaged in the business of producing oil in Wichita County, Texas, and in that vicinity in 1919 paid no excess profits tax at all.

CHART

TOO

LARGE

FOR

FILMING

For these reasons, as well as those heretofore urged in previous claims, this company asks for the refund of the amount above indicated.

(Here follows Exhibit "C", marked side folio pages 54 and 54½)

[fol. 55] The Burk-Waggoner Oil Association, the taxpayer making this report, claims the benefit of Sections 327 and 328 of the Revenue Act of 1918, and that its tax liability should be reduced as therein provided for, and in accordance with the application for special assessment herein made, and pays the sum of $138,150.51, the first quarterly installment of its 1919 tax computed without the benefit of said special assessment under protest and only to avoid the self-executing penalties imposed by the Statutes.

[fol. 56] STATE OF TEXAS,
County of Wichita:

We, the undersigned, R. M. Waggoner, President, and Clois L. Greene, Secretary-Treasurer, of the Burk-Waggoner Association of Wichita Falls, Texas, being duly sworn on oath severally state.

That the statement of facts contained in the Schedules, Statements, Maps and other data submitted in connection with the Income Tax Return for the year 1919 of the Burk-Waggoner Oil Association of Wichita Falls, Texas, are true.

(Signed) R. M. Waggoner, Clois L. Greene.

Subscribed and sworn to before me on this the 5th day of March, A. D. 1920. Harry C. Weeks, Notary Public in and for Wichita County, Texas. (Seal.)

[fol. 57] Statement and Schedules Attached to the Income and Profits Tax Return of the Burk-Waggoner Oil Association for the Calendar Year 1919

Statement of Deductions Shown on Line 12, Schedule A

Labor employed in drilling and operating property	$2,907.20
Fuel and Water	9,573.41
Hauling	2,379.75
Office and Overhead Expense (including salaries of book-Keepers, stationary, office rent, and miscellaneous items)	3,693.45
Miscellaneous expense (including an attorney's fee of $5,000.00)	6,791.00
Total	$30,437.61

Statement under Schedule A-22

The Burk-Waggoner Oil Association sold its properties to A. D. Morton on or about May 5, 1919, for a consideration of two million dollars of which $1,250,000.00 was paid in cash and $750,000.00 in notes. This property had been taken into the company for the price [fol. 58] of $40,000.00 and the company had expended in the development of same $111,227.10, which may be subdivided under the following general items:

Investment for 1918

Lease equipment	2,592.85
Paid for drilling in 1918	8,000.00
Total	10,592.85

None of the items above shown were charged to expense in 1918.

Investment for 1919

General Equipment	3,280.25
Lease Equipment	53,364.45
Drilling	43,988.95
Total for 1919	100,634.25
Total Investment	111,226.50

Upon this sale the Burk-Waggoner Oil Association paid to the agents handling same a commission of $50,000.00, and to the attorneys preparing the contract relative to same a fee of $5,000.00. The depletion item of $19,715.44 is the same claim in Schedule A and the net profit in this transaction is $1,813,488.94.

There is attached hereto and made a part of this report, a copy of the original Articles of Association of the Burk-Waggoner Oil Association; a copy of the assignment of the lease to the Burk-Waggoner Oil Association; and a copy of the assignment by the Burk- [fol. 59] Waggoner Oil Association to A. D. Morton. From the last instrument it will be seen that in addition to the $2,000,000.00 consideration the Burk-Waggoner Oil Association was to be reimbursed for certain developments which they had already begun on the lease. The amount received by the Burk-Waggoner Oil Association on this account is included in Item One of Schedule A.

Statement Relative to Claim for Benefit of New Discovery under Schedule A-19 and Schedule D-4

The Burk-Waggoner Oil Association claims the benefit of Sections 234 (9) and 337 of the Excess Profits Tax Law, claiming the benefit of a discovery both for the purpose of depletion and a sale and in regard to this they refer to the original assignment to the Burk-Wag-

goner Oil Association above shown and to other papers hereinafter referred to.

A map, drawn on a scale of 400 feet to one inch is submitted herewith locating the holdings of the Burk-Waggoner Oil Association, about which the following explanation is made.

Well No. One shown thereon was completed on April 21, 1919 at a depth of approximately 1,688 feet. At that time no well was producing, or had ever produced, from that depth within a vicinity of [fol. 60] several miles, and at the time the Burk-Waggoner Oil Association acquired this lease, as well as at the time the first well was completed, this territory was strictly "wild cat." Well No. 1 had an initial production of approximately 2,000 barrels per day and it proved the commercial value of this lease and caused a great enhancement in value as will be seen from the sale made within less than thirty days. At the time of this sale wells Nos. 2, 3 and 10, shown on said map, were drilling. The other wells, with the exception of well No. 1 which was producing, were merely locations or derricks. For the purpose of depletion a valuation of $2,000,000.00 upon the entire lease is claimed and a depletion unit of $1.00 per barrel is claimed. It being estimated that this lease had a potential production of 2,000,000.00 barrels.

There is also attached hereto a map of this district of the Wichita County Oil Fields and there is a line drawn around this property which encloses the area in which there were no producing wells at the time the Burk-Waggoner Association's Well No. 1 was completed to-wit: April 21, 1919. A log of the well is also submitted.

During the period from the completion of this well until date of the sale, above referred to, the Burk-Waggoner Oil Association produced 19,715.44 barrels of oil.

The lease cost the Burk-Waggoner Oil Association $40,000.00 as is above shown.

[fol. 61] Statement under Schedule G-2

An oil and Gas lease paid for in stock is carried as an asset by the Burk-Waggoner Oil Association. It was acquired on November 15, 1918. Forty Thousand Dollars par value of the Burk-Waggoner Oil Association stock was paid for same. The actual cash value of the property at that time was approximately $40,000.00. This valuation is determined from the valuation of surrounding property and the potential value of same. The Burk-Waggoner Oil Association kept no books merely a record of receipts and disbursements so no valuation is shown upon the company's books for the lease.

Statement under Schedule G-3

The only change in ownership of the property held by the Burk-Waggoner Oil Association was the sale of the oil and gas lease made by the promoters of the company to the company at the date of its organization, to-wit, November 15, 1918. The capital stock of the

Burk-Waggoner Association was fixed at $60,000.00 and the promoters of the company received $40,000.00 of the capital stock for this lease. Not all of this stock was issued to them, as they intended at all times to sell a large part of the stock that they received, and they had a part of same sold and the remainder of the stock issued to them so that while immediately after the organization of the com-
[fol. 62] pany more than fifty per cent of the stock was in the hands of the promoters, who owned the property before the organization, it did not remain in their hands for any length of time.

The construction placed upon this becomes immaterial, however, in view of the fact that the Burk-Waggoner Oil Association is entitled to the benefit of the twenty per cent provision in computing its Excess Profits Tax. The lease originally cost them (the promotors) $125.00 per acre.

Statement under Schedule X

No books were kept by the Burk-Waggoner Oil Association, merely a record of receipts and disbursements, so balance sheets for the beginning and end of the period cannot be submitted.

Statement under Schedule L

The Company had no surplus at the beginning of the taxable year. Its total net profits for the year were $1,838,053.90. There were no other credits to surplus. The company paid dividends during 1919 amounting to $1,250,000.00.

[fol. 63] Statement under Schedule D-4

Total Excess Profits Tax	$731,334.02
Portion Attributable to Sale	721,559.99
Portion Attributable to other Operations	9,774.03
Maximum Tax Limitations on account of Sale	400,000.00
Total Excess Profits Tax	409,774.03

[fol. 64] Log of Well No. 1, Burk-Waggoner Oil Asso., R. M. Waggoner Lands, Block 84, Red River Valley Lands, Wichita County, Texas

Casing Record

59 feet	15½ inch.
496 "	12½ "
915 "	10 "
1,186 "	8 "
1,162 "	6⅝ "

(Computed April 4, 1919.)

Begun in December, 1918

Surface.

Surface	0	to	37
Water Sand	37	"	50
Red Shale	50	"	150
Light Brown Shale	150	"	175
Red Shale	175	"	410
Water Sand	410	"	420
Red Shale	420	"	550
Light Brown Shale	550	"	625
Red Shale	625	"	665
Lime Shell	665	"	670
Red Shale	670	"	735
Water Sand	735	"	745
Red Shale	745	"	810
Blue Shale	810	"	875
Red Shale	875	"	880
Blue Shale	880	"	895
Red Shape	895	"	925
Blue Shale	925	"	935
Water Sand	935	"	950
Red Shale	950	"	955
Water Sand	955	"	1030
Blue Shale	1030	"	1035
[fol. 65] Red Shale	1035	"	1040
Light Brn. Shale	1040	"	1065
Red Shale	1065	"	1100
Water Sand	1100	"	1115
Blue Shale	1115	"	1125
Red Shale	1125	"	1130
Blue Shale	1130	"	1170
Water Sand	1170	"	1200
Red Shale	1200	"	1230
Light Brn. Shale	1230	"	1275
Light Blue Shale	1275	"	1285
Lime *Shell*	1285	"	1290
Blue Shale	1290	"	1295
Red Shale	1295	"	1300
Blue Shale	1300	"	1315
Red Shale	1315	"	1370
Blue Shale	1370	"	1385
Lime Shale	1385	"	1390
Blue Shale	1390	"	1395
Red Shale	1395	"	1400
Blue Shale	1400	"	1415
Water Sand	1415	"	1450
Blue Shale	1450	"	1520
Water Sand	1520	"	1525
Sandy Lime	1525	"	1528
Blue Shale	1528	"	1590

Surface

Sandy Lime	1590	to	1595
Red Shale	1595	"	1610
[fol. 66] Blue Shale	1610	"	1658
Oil Sand	1658	"	1688

[fol. 67] Copy

STATE OF TEXAS,
County of Wichita:

Know All Men By These Presents: That we, C. F. Wilson, Henry Evans, D. H. Milton, O. P. Darsey, Clois L. Greene, W. H. Anchor, E. H. Pigg, J. P. Crenshaw, A. P. Howard, R. M. Waggoner, Lee Crenshaw and A. H. Murchison for and in consideration of the sum of $1,000.00 and other good and valuable consideration cash in hand paid by R. M. Waggoner, Clois L. Green, Lee Crenshaw, W. H. Anchor and A. H. Murchison, Trustees for the Burk-Waggoner Oil Association, a joint stock association, the receipt of which is hereby acknowledged and confessed, have granted, sold, conveyed and assigned and by these presents do grant, sell, convey and assign unto the said R. M. Waggoner, Clois L. Greene, Lee Crenshaw, W. H. Anchor and A. H. Murchison, Trustees all our rights, title and interest in and to that certain lease and leasehold estate covering 60 acres of land in the form of a square in the Northeast corner of Block 84 of the Red River Valley Lands Subdivision of Wichita County, Texas, the Northeast corner of said Block 84 being a part of the lands covered by lease of R. M. Waggoner and wife to the grantors herein dated September 6, A. D. 1918, and recorded in Volume 109, page 26-27 of the Deed Records of Wichita County, Texas, reference to which is here made for full particulars.

To have and to hold unto the said R. M. Waggoner, Clois L. Greene, Lee Crenshaw, W. H. Anchor and A. H. Murchison, Trustees and their successors and assigns forever, subject to the terms, conditions and stipulations of the original lease contract above referred to which terms and conditions and stipulations are assumed by the Grantees herein.

[fol. 68] Witness our hands on this 14th day of December, A. D. 1918.

Lee Crenshaw, W. H. Anchor, D. H. Milton, Clois L. Greene, A. H. Murchison, E. H. Pigg, A. P. Howard, M. D., C. F. Wilson, R. M. Waggoner, L. P. Crenshaw, O. P. Darsey, Henry Evans.

Acknowledgments

STATE OF TEXAS,
County of Wichita:

Before me, the undersigned a Notary Public, in and for Wichita County, State of Texas, on this day personally appeared D. H. Milton, W. H. Anchor, L. P. Crenshaw, R. M. Waggoner and Lee

Crenshaw, known to me to be the persons whose names are subscribed to the foregoing instrument, and acknowledged to me that they executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 17th day of December, A. D. 1918. A. L. Huey, Notary Public, Wichita County, Tex. (Seal.)

STATE OF TEXAS,
County of Wilbarger:

Before me, the undersigned, a Notary Public in and for the County and State aforesaid on this day personally appeared A. H. Murchison, Clois L. Greene, E. H. Pigg, and A. P. Howard known to me to be the persons whose names *is* subscribed to the foregoing instrument and acknowledged to me that they executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 16th day of December, A. D. 1918. C. V. King, Notary Public, Wilbarger County, Texas. (Seal.)

[fol. 69] STATE OF TEXAS,
County of Wichita:

Before me, the undersigned authority, in and for Wichita County, Texas, on this day personally appeared C. F. Wilson, known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this the 17th day of December, A. D. 1918. Dave Thorne, J. P. and ex-Officio Notary Public, Wichita County, Texas. (Seal.)

STATE OF TEXAS,
County of Floyd:

Before me, Kenneth Bain a Notary Public in and for said County and State on this day personally — O. P. Darsey, known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this 19th day of December, 1918. Kenneth Bain, Notary Public. (Seal.)

STATE OF TEXAS,
County of Eastland:

Before me, Connie Davis, a Notary Public in and for Eastland County, Texas, on this day personally appeared Henry Evans known to me to be the person whose name is subscribed to the foregoing

instrument, and acknowledged to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office this 21st day of De-
[fol. 70] cember, A. D. 1918. Connie Davis, Notary Public, Eastland County, Texas. (Seal.)

Filed for record December 26th, 1918 at 3:19 P. M.
Recorded January 1st, 1919, at 8:55 A. M.
W. T. Harris, Clerk County Court Wichita County, Texas, by —— ——, Deputy.

[fol. 71] Wichita Falls, Texas, March 5th, 1920.

Honorable Daniel C. Roper,
Commissioner of Internal Revenue,
Washington, D. C.

SIR:

The Burk-Waggoner Oil Association, a joint stock association of Wichita Falls, Texas, hereby makes application for a special assessment of its excess profits tax for the calendar year of 1919, under the terms and provisions of Section 327 of the 1918 income and excess profits tax act, and submits that if its tax be determined without the benefit of this Section, it would, *owning* — the abnormal conditions affecting the capital and income of the Association, wor*th* upon the Association an exceptional hardship evidenced by gross disproportion between the tax computed without the benefit of this Section and the tax computed by reference to representative concerns specified in Section 328 and in support of this application submits the following in accordance with regulations 45:

It will be recalled that the present Revenue Act was re-written in conference and the bills, as they had passed the House and Senate, were re-worded. As passed by the Senate, Section 327 contained a more specific enumeration of the classes of special cases than did the Section when it came out of conference. The Senate Bill contained the following: "(e) Where the invested capital is materially disproportionate to the net income, as compared with representative corporations engaged in a like or similar trade or business because (3) the net income for the taxable year is abnormally high due to the realization in onr year of (a) gains, profits or income earned or accrued during a period of years of (b) extraordinary *or* profits derived from the sale of property, the principal value of which has [fol. 72] been demonstrated by prospecting of exploration and discovery work done by the tax-payer."

Senator Simmons in introducing the conference report to the Senate said (congressional record page 3776 Feb. 17th, 1919) "The relief provisions (i. e. of Section 327) as contained in the Senate Amendments, were specific in their terms the general opinion of the conference and of the Department, and I concur in that opinion, is that the Amendment, as redrafted, broadens rather than restrains the powers of the Commissioner in the matter of relief against injustice, inequality and discrimination."

On December 19th, 1919, inquiry was addressed to the Commissioner, relative to the application of this Section to the Burk-Waggoner Oil Association, inquiry having been made by W. G. McAdoo of the firm of McAdoo, Cotton & Franklin, Attorneys, and on January 6th, 1920, a reply to this inquiry was received to the effect that because a Company received the benefit of Section 337 it would not thereby be deprived of the benefit of Sections 327 and 328, if it were found upon examination to be otherwise entitled to a Special assessment.

For the convenience of the Department it is stated that reference memorandum upon the letter was IT:T:RR AM.

As will be seen from the attached return made by the Burk-Waggoner Oil Association, its excess profits tax for the year 1919 without the benefits of Sections 327 and 328 exceeds $100,000.00. Its capital is $60,000.00, or in other words, the excess profits tax is more than 660 per cent of its capital stock. It requires but a glance at the return to show that this tax is due almost solely to the profit derived [fol. 73] from the sale of its oil producing property. This oil producing property, as will be seen from other information submitted with this return, was acquired in 1918, at a nominal value and the Burk-Waggoner Oil Association raised the funds to develop same for oil, and on April 21, 1919, discovered oil in large quantities thereon; thereby proving a territory in which for an area of several miles around the well no oil had ever been discovered and thereby opening up what is probably the greatest oil field ever discovered in America. There can be no question but what it made a new discovery both from the standpoint of the oil operator and from the Department standpoint, as stated in its rulings.

This, then, brings the Burk-Waggoner Oil Association directly within one of the special relief provisions, as contained in the Senate draft of the Revenue Bill where it is said, as above quoted "extraordinary gain or profit derived from the sale of property, the principal value of which has been demonstrated by prospecting or explorations and discovery work done by the tax payer." If, as Senator Simmons says, this provision, as redrafted in conference is broadened, there can be no question but that the Burk-Waggoner Oil Association is entitled to this relief if its excess profits tax, as computed without the benefit of Sections 327 and 328 is grossly disproportionate to the tax of representative corporations specified in 328.

It appears almo*t*s axiomatic that representative corporations engaged in the business of producing oil and gas do not ordinarily earn profits upon which they would have to pay a tax exceeding six times their capital stock.

The published reports of the larger oil producing companies, like the various Standard Oil Companies, The Texas Company, Magnolia Petroleum Company, Gulf Producing Company and the Sinclair [fol. 74] Companies will show that the larger companies do not earn on their invested capital anything approximating one hundred per cent, and we are sure that an examination of the reports of any of these companies will show that their tax is only a small percentage of their invested capital, but it would probably be unfair to compare

the instant case with these larger concerns for they operate extensively in various sections of the country and the hazard of the business is reduced to an average by the wide scope of their operations, so we are not submitting any figures relative to these larger companies.

We have selected from the smaller companies operating exclusively in the Burkburnett, Wichita County, Texas, oil fields, seven companies, whose capital is of approximately the same size of the Burk-Waggoner Oil Association and whose history covers approximately the same period. In selecting these companies we have endeavored to select the most successful companies operating in the district, and we submit that an average of all of the companies would show a much smaller percentage of tax to capital. A large number of successful concerns operating in this field operate as partnerships and for that reason their returns cannot be compared with the Burk-Waggoner Oil Association. Among these might be included the Fowler Farm Oil Company, the United Producers, and several others.

There is attached hereto a statement of the income expense and tax liability for the year 1919, of these seven concerns, and in addition to this statement, the following explanation is made regarding them:

The Western Globe Oil Company owns an oil and gas lease on ten acres of land adjacent to the Burk-Waggoner Oil Association property. It made what is commonly known as a fifty-fifty drilling contract with the Humble Oil & Refining Company, whereby it re- [fol. 75] ceived fifty per cent of the oil produced, and the Humble Oil & Refining Company drilled the wells and paid the operating expense; for that reason no expense is shown.

The Golconda Oil Company No. One; the Texas Chief Oil Company; the Victory Petroleum Company; Green River Oil Company and the Woodrow-Lee Oil Company were all organized at or about the time the Burk-Waggoner Oil Association was organized. The Adams Oil Company is one of the older companies, having been organized in 1917, and its property being in the old Burkburnett field.

In the statement shown it is not attempted to make proper allowance for depreciation and depletion; the statement shows gross income and operating expense without any allowance for these items, and for this reason, of course, the tax, as shown, is considerably larger than it will be when proper allowance is made for these deductions.

Information shown in the statement is submitted as reliable and accurate with these qualifications. Some of the statements were taken from published reports of the companies and the remainder were secured from officials of the various companies.

Your particular attention is called to the fact that the average excess profits tax paid by these companies will be $46,880.88 each, and that this tax is $86.35 per cent of the average invested capital of these concerns. The Golconda Oil Company No. One, the most successful of those shown, will pay an excess profits tax equal to 270.43 per cent of its capital stock. If the excess profits tax of the Burk-Waggoner Oil Association be reduced to the average shown it

STATEMENT O

REPRESENTATIVE
BUSINESS O
OIL

ORGANIZED	Name and Address	Capital	
1919	Western Globe Oil Co.: Wichita Falls, Tex:	$55000.00	
1919	Golconda Oil Co.#1 : Wichita Falls, Texas:	65000.00	
1919	Texas Chief Oil Co. : Wichita Falls, Texas :	80000.00	
1917	Adams Oil Company, : Wichita Falls, Texas :	50000.00	
1918	Victory Petroleum Co : Wichita Falls, Texas.:	30000.00	
1918	Green River Oil Co. : Wichita Falls, Texas :	30000.00	
1918	Woodrow-Lee Oil Co. : Wichita Falls, Texas:	70000.00	
		380000.00	
	AVERAGE----------	54285.71	

TEMENT OF THE INCOME EXPENSE AND TAX LIABILITY
FOR THE YEAR 1919 OF
NTATIVE CORPORATIONS AND ASSOCIATIONS ENGAGED IN THE
INESS OF PRODUCING OIL IN THE WICHITA COUNTY
OIL FIELDS

ital	Gross Income	Expense	Net Income	Excess Profits Tax	Income Tax	Total Tax	Percentage of Excess Profits Tax to Capital
00.00	$37622.00		$37622.00	$11768.80	$2585.32	$14354.12	21.39
00.00	498499.01	$46049.01	452449.70	175779.78	27466.98	203246.86	270.43
00.00	227828.73	48828.37	179000.00	66520.00	11240.00	77760.00	83.15
00.00	98118.08	30106.05	68012.03	22448.12	4556.39	27004.51	44.89
00.00	78394.67	20865.97	57528.70	14411.48	4311.72	18723.20	48.04
00.00	131462.85	54692.25	76770.60	26108.24	5066.24	31174.48	87.02
00.00	78011.84	38687.35	39324.49	11129.80	2819.47	13949.27	16.89
00.00	1149937.18	239229.30	910707.52	328166.22	58046.12	386212.44	
85.71	164276.74	34174.70	130101.07	46880.88	8292.30	55173.20	86.35

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would amount to $51,810; if it were reduced to the highest rate shown it would amount to $162,258.00.

[fol. 76] We submit that no further showing than that above made is necessary to prove conclusively that the excess profits tax of the Burk-Waggoner Oil Association as computed without the benefit of the Sections above referred to is grossly disproportionate to that of representative concerns engaged in the same business.

The only business conducted by the Burk-Waggoner Oil Association was that of producing oil, as above stated. It was organized in 1918 for the purpose of developing the 60 acre tract more fully described in the attached papers. It sold a small amount of its capital to the investing public, thereby securing funds to develop the property, drilled one well thereon, which produced oil in large quantities and then a few days thereafter sold its property for Two Million Dollars. This is the only business ever conducted by the Burk-Waggoner Oil Association. The Burk-Waggoner Oil Association had no net income for any period other than for the year 1919. Its invested capital at the date of its organization was $40,000.00, and at the end of the year 1918, $45,000.00. The Burk-Waggoner Oil Association derived no gains, profits, commissions or other income on account of government contracts of any kind whatsoever.

Respectfully submitted, McAdoo, Cotton & Franklin, Weeks, Morrow, Weeks & Francis, Attorneys for the Burk-Waggoner Oil Association. HCW:B.

(Here follow statements, marked side folio pages 77, 78, and 78½)

[fol. 79] This is a corrected report of Burk-Waggoner Oil Association, Wichita Falls, Texas, and corrects original Report for year 1919 filed by said company.

(Here follows Exhibit D, marked side folio pages 80 and 80½)

[fol. 81] Statements and Schedules Attached to the Income and Profits Tax Return of the Burk-Waggoner Oil Association for the Calendar Year 1919

Statement of Deductions Shown on Line 12, Schedule "A"

Labor employed in drilling and operating property	$2,907.20
Fuel and Water	9,573.41
Hauling	2,379.75
Office and overhead expense (including salaries of bookkeepers, stationery, office rent and miscellaneous items)	3,693.45
Miscellaneous expense (including an attorney fee of $5,000.00)	6,791.00
Total	$30,437.61

Statement under Schedule G-2

An oil and gas lease paid for in stock is carried as an asset by the Burk-Waggoner Oil Association. It was acquired on November 15, 1918. Forty Thousand Dollars par value of the Burk-Waggoner Oil Association stock was paid for same. The actual cash value of the property at that time was approximately $40,000.00. This valuation is determined from the valuation of surrounding property and the potential value of same. The Burk-Waggoner Oil Association kept no books—merely a record of receipts and disbursements, so no valuation is shown upon the company's books for the lease.

Statement under Schedule G-3

The only change in ownership of the property held by the Burk-Waggoner Oil Association was the sale of the oil and gas lease made [fol. 82] by the promoters of the Company to the Company at the date of its organization, to-wit, November 15, 1918. The capital stock of the Burk-Waggoner Oil Association was fixed at $60,000.00 and the promoters of the Company received $40,000.00 of the capital stock for this lease. Not all of this stock was issued to them, as they intended at all times to sell a large part of the stock that they received, and they had a part of same sold and the remainder of the stock issued to them so that while immediately after the organization of the company more than fifty per cent of the stock was in the hands of the promoters, who owned the property before the organization, it did not remain in their hands for any length of time.

Statement under Schedule X

No books were kept by the Burk-Waggoner Oil Association,—merely a record of the receipts and disbursements, so balance sheets for the beginning and end of the period cannot be submitted.

[fol. 83] Statement under Schedule A-22

The Burk-Waggoner Oil Association sold its properties to A. D. Morton on or about May 5th, 1919, for a consideration of $2,000,000.00, of which $1,250,000.00 was paid in cash and $750,000.00 in notes. This property had been taken into the Company for the price of $40,000.00 and the Company had expended in the development of same $111,227.10, which may be subdivided under the following general items:

Investment for 1918:

Lease equipment	$2,592.85	
Paid for drilling in 1918	8,000.00	
Total		$10,592.85

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Investment for 1919:

General equipment	3,280.25	
Lease equipment	53,364.45	
Drilling	43,989.95	
Total for 1919		100,634.25
Total investment		$111,226.50

Upon this sale the Burk-Waggoner Oil Association paid to the agents handling same a commission of $50,000.00 and to the attorneys preparing the contract relative to same a fee of $5,000.00. Depletion of $19,715.44 had been charged off.

The net enhancement in value of the capital assets realized by this sale is $1,813,488.94. This is not included in calculating net income for the reason that it is the contention of the taxpayer that this gain or enhancement in value is not taxable income for the reasons more fully set forth in the Claims for Abatement and Refund filed herewith.

[fol. 84] Statement Relative to Claim for Benefit of Discovery under Schedule A-19

The Burk-Waggoner Oil Association claims the benefit of Section 234, (9), claiming the benefit of discovery for the purpose of depletion, and in this connection, reference to all of the Exhibits attached to the original report made by the Burk-Waggoner Oil Association.

Statement under Schedule L

The Company had no surplus at the beginning of the taxable year. Its net profits, not including the gain or enhancement in value of its capital assets derived from the sale above referred to, is $24,564.96. If it should be held that this gain or enhancement in value should be included, the total net profits would be $1,838,053.90. The Company paid liquidating dividends during 1919 amounting to $1,250,000.00.

(Here follows statement, marked side folio pages 85 and 85½)

[fol. 86] "Exhibit E"

Form 1107

Treasury Department, United States Internal Revenue

Taxpayer's Receipt for Income and Excess Profits Tax

Office Collector Internal Revenue

Notice to Taxpayer

Before presenting payment to cashier enter on this form—

(a) Name.
(b) Address.
(c) Form Number of Return.
(d) Amount of Tax Paid.

Form No. of return—Apr.—404,912—1920 List.
Tax, $145,827.67.
Name: Burk-Waggoner Oil Association.
Address: Wichita Falls, Texas.
Payment made under protest.

Received payment. Paid: Date, 3/28/22.
Geo. C. Hopkins, Collector. LAP.

[fol. 87] "Exhibit F"

Treasury Department, Internal Revenue Service, Dallas, Tex.

IT. BG. March 22, 1922.

Burk-Waggoner Oil Association, Wichita Falls, Texas.

Sirs: Reference is made to your 1919 income tax account appearing under serial number April 404912 of the 1920 List, against which an Abatement claim was filed by you in the amount of $138,150.49.

The Commissioner of Internal Revenue, Washington, D. C. reported to this office on January 15, 1922, that your claim had been allowed for $200.00 and rejected for $137,950.49. Notice and demand for the tax, plus interest to January 15th, was at that time mailed to you by this office.

To-date, the records do not show that payment has been received, and your account now stands as follows:

Tax	$137,950.49
5% Penalty	6,897.53
Int. 9 Mo. to 1-15-22 @ ½%	6,207.78
Int. from 1-15-22 to 3-15 @ 1%	2,759.00
Total	$153,814.80

Warrant for Distraint is today being issued for the above amount and placed in the hands of Field Office with instructions to collect the tax.

Respectfully, Geo. C. Hopkins, F. H., Collector. LAP.

[fol. 88] "EXHIBIT G"

IT:SA:NR:A CRU-404912 Nov. 26, 1921.

Burk-Waggoner Oil Association, Wichita Falls, Texas.

Sirs: Your claims for the refunding of $407,491.65, and the abatement of $138,150.49, corporation income and profits tax for the calendar year 1919, have been examined.

The bases of your claims, as presented in written arguments, numbered one to six, inclusive, appearing thereon, have been considered.

It is to be noted that since the filing of your claims the Supreme Court of the United States has rendered, on different occasions, decisions against questions similar to those embodied in your claims.

An audit of the original returns as filed, discloses an overpayment of tax of $200.00 for the calendar year 1919 due to your failure to use the $2,000.00 exemption in computing the amount of net income subject to the 10% normal tax. The correct tax is found to be $552,402.02, whereas $552,602.02 tax has been assessed on the original returns as filed.

As your claims have been adjusted in accordance with the foregoing computations, your claim for the refunding of $407,491.65 will be rejected and your claim for the abatement of $138,150.49 will be allowed for $200.00 and rejected for $137,950.49 in the next Schedule to be approved by this Bureau.

Respectfully, ——— ———, Commissioner. LMM.

[fol. 89] EXHIBIT TO BILL OF EXCEPTIONS

Wichita Falls, Texas, March 5th, 1920.

Honorable Daniel C. Roper, Commissioner of Internal Revenue, Washington, D. C.

Sir: The Burk-Waggoner Oil Association, a joint stock association of Wichita Falls, Texas, hereby makes application for a special assessment of its excess profits tax for the calendar year of 1919, under the terms and provisions of Section 327 of the 1918 income and excess profits tax act, and submits that if its tax be determined without the benefit of this Section, it would, owning — the abnormal conditions affecting the capital and income of the Association, worth upon the Association an exceptional hardship evidenced by gross disproportion between the tax computed without the benefit of this Section and the tax cumputed by reference to representative concerns

specified in Section 328 and in support of this application submits the following in accordance with regulations 45;

It will be recalled that the present Revenue Act was re-written in conference and the bills, as they had passed the House and Senate, were re-worded. As passed by the Senate, Section 327 contained a more specific enumeration of the classes of special cases than did the Section when it came out of conference. The Senate Bill contained the following: "(e) Where the invested capital is materially disproportionate to the net income, as compared with representative corporations engaged in a like or similar trade or business because (3) the net income for the taxable year is abnormally high due to the realization in one year of (a) gains, profits or income earned or accrued during a period of years of (b) extraordinary *or* profits derived from the sale of property, the principal value of which has [fol. 90] been demonstrated by prospecting of exploration and discovery work done by the tax-payer."

Sen*i*-or Simmons in introducing the conference report to the Senate said (congressional record page 3776 Feb. 17th, 1919): "The relief provisions (i. e. of Section 327) as contained in the Senate Amendments, were specific in their terms the general opinion of the conference and of the Department, and I concur in that opinion, is that the Amendment, as redrafted, broadens rather than restrains the powers of the Commissioner in the matter of relief against injustice, inequality and discrimination."

On December 19th, 1919, inquiry was addressed to the Commissioner, relative to the application of this Section to the Burk-Waggoner Oil Association, inquiry having been made by W. G. McAdoo of the firm of McAdoo, Cotton & Franklin, Attorneys, and on January 6th, 1920, a reply to this inquiry was received to the effect that because a company received the benefit of Section 337 it would not thereby be deprived of the benefit of Sections 327 and 328, if it were found upon examination to be otherwise entitled to a special assessment.

For the convenience of the Department it is stated that reference memorandum upon the letter was IT:T:RR AM.

As will be seen from the attached return made by the Burk-Waggoner Oil Association, its excess profits tax for the year 1919 without the benefits of Sections 327 and 328 exceeds $400,000.00. Its capital is $60,000.00, or in other words, the excess profits tax is more than 660 per cent of its capital stock. It requires but a glance at the return to show that this tax is due almost solely to the profit [fol. 91] derived from the sale of its oil producing property. This oil producing property, as will be seen from other information submitted with this return, was acquired in 1918, at a nominal value and the Burk-Waggoner Oil Association raised the funds to develop same for oil, and on April 21, 1919, discovered oil in large quantities thereon; thereby proving a territory in which for an area of several miles around the well no oil had ever been discovered and thereby opening up what is probably the greatest oil field ever discovered in America. There can be no question but what it made a new discovery both from the standpoint of the oil operator and from the Department standpoint, as stated in its rulings.

This, then, brings the Burk-Waggoner Oil Association directly within one of the special relief provisions, as contained in the Senate draft of the Revenue Bill where it is said, as above quoted "extraordinary gain or profit derived from the sale of property, the principal value of which has been demonstrated by prospecting or explorations and discovery work done by the tax payer." If, as Senator Simmons says, this provision, as redrafted in conference is broadened, there can be no question but that the Burk-Waggoner Oil Association is entitled to this relief if its excess profits tax, as computed without the benefit of Sections 327 and 328 is grossly disproportionate to the tax of representative corporations specified in 328.

It appears almots axiomatic that representative corporations engaged in the business of producing oil and gas do not ordinarily earn profits upon which they would have to pay a tax exceeding six times their capital stock.

The published reports of the larger oil producing companies, like the various Standard Oil Companies, The Texas Company, Magnolia Petroleum Company, Gulf Producing Company and the Sinclair Companies will show that the larger companies do not earn on their [fol. 92] invested capital anything approximating one hundred per cent, and we are sure that an examination of the reports of any of these companies will show that their tax is only a small percentage of their invested capital, but it would probably be unfair to compare the instant case with these larger concerns for they operate extensively in various sections of the country and the hazard of the business is reduced to an average by the wide scope of their operations, so we are not submitting any figures relative to these larger companies.

We have selected from the smaller companies operating exclusively in the Burkburnett, Wichita County, Texas, oil fields, seven companies, whose capital is of approximately the same size of the Burk-Waggoner Oil Association and whose history covers approximately the same period. In selecting these companies we have endeavored to select the most successful companies operating in the district, and we submit that an average of all of the companies would show a much smaller percentage of tax to capital. A large number of the successful concerns operating in this field operate as partnerships and for that reason their returns cannot be compared with the Burk-Waggoner Oil Association. Among these might be included the Fowler Farm Oil Company, the United Producers, and several others.

There is attached hereto a statement of the income expense and tax liability for the year 1919, of these seven concerns, and in addition to this statement, the following explanation is made regarding them:

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The Golconda Oil Company No. One; the Texas Chief Oil Company; the Victory Petroleum Company; Green River Oil Company and the Woodrow-Lee Oil Company were all organized at or about the time the Burk-Waggoner Oil Association was organized. The Adams Oil Company is one of the older companies, having been organized in 1917, and its property being in the old Burkburnett field.

In the statement shown it is not attempted to make proper allowance for depreciation and depletion; the statement shows gross income and operating expense without any allowance for these items, and for this reason, of course, the tax, as shown, is considerably larger than it will be when proper allowance is made for these deductions.

Information shown in the statement is submitted as reliable and accurate with these qualifications. Some of the statements were taken from published reports of the companies and the remainder were secured from officials of the various companies.

Your particular attention is called to the fact that the average excess profits tax paid by these companies will be $46,880.88 each, and that this tax is 86.35 per cent of the average invested capital of these concerns. The Golconda Oil Company No. One, the most successful of those shown, will pay an excess profits tax equal to 270.43 per cent of its capital stock. If the excess profits tax of the Burk-Waggoner Oil Association be reduced to the average shown it would amount to $51,810; if it were reduced to the highest rate shown it would amount to $162,258.00.

[fol. 94] We submit that no further showing than that above made is necessary to prove conclusively that the excess profits tax of the Burk-Waggoner Oil Association as computed without the benefit of the Sections above referred to is grossly disproportionate to that of representative concerns engaged in the same business.

The only business conducted by the Burk-Waggoner Oil Association was that of producing oil, as above stated. It was organized in 1918 for the purpose of developing the 60 acre tract more fully described in the attached papers. It sold a small amount of its capital to the investing public, thereby securing funds to develop the property, drilled one well thereon, which produced oil in large quantities and then a *few* days thereafter sold its property for Two Million Dollars. This is the only business ever conducted by the Burk-Waggoner Oil Association. The Burk-Waggoner Oil Association had no net income for any period other than for the year 1919. Its invested capital at the date of its organization was $40,000.00, and at the end of the year 1918, $45,000.00. The Burk-Waggoner Oil Association derived no gains, profits, commissions or other income on account of government contracts of any kind whatsoever.

Respectfully submitted, McAdoo, Cotton & Franklin, Weeks, Morrow, Weeks & Francis, Attorneys for the Burk-Waggoner Oil Association. HCW:B.

(Here follows Exhibit to Bill of Exceptions marked side folio page 95)

Exhibit B

STATEMENT OF THE I

FOR THE

REPRESENTATIVE CORPORA

BUSINESS OF PRODUCI

OIL FIELDS

ORGANIZED	Name and Address	Capital	Gross In
1919	Western Globe Oil Co.: Wichita Falls, Tex:	$55000.00	$37622.00
1919	Golconda Oil Co.#1 : Wichita Falls, Texas:	65000.00	498499.01
1919	Texas Chief Oil Co. : Wichita Falls, Texas :	80000.00	227828.78
1917	Adams Oil Company, : Wichita Falls, Texas :	50000.00	98118.08
1918	Victory Petroleum Co : Wichita Falls, Texas.:	30000.00	78394.67
1918	Green River Oil Co. : Wichita Falls, Texas :	30000.00	131462.85
1918	Woodrow-Lee Oil Co. : Wichita Falls, Texas:	70000.00	78011.84
		380000.00	1149937.18
	AVERAGE----------	54285.71	164276.74

Ecclectic Bell of Exchanges

ATEMENT OF THE INCOME EXPENSE AND TAX LIABILITY
FOR THE YEAR 1919 OF
ENTATIVE CORPORATIONS AND ASSOCIATIONS ENGAGED IN THE
SINESS OF PRODUCING OIL IN THE WICHITA COUNTY
OIL FIELDS

pital	Gross Income	Expense	Net Income	Excess Profits Tax	Income Tax	Total Tax	Percentage of Excess Profits Tax to Capital
000.00	$37622.00		$37622.00	$11768.80	$2585.32	$14354.12	21.39
000.00	498499.01	$46049.01	452449.70	175779.78	27466.98	203246.86	270.43
000.00	227828.73	48828.37	179000.00	66520.00	11240.00	77760.00	83.15
000.00	98118.08	30106.05	68012.03	22448.12	4556.39	27004.51	44
000.00	78394.67	20865.97	57528.70	14411.48	4311.72	18723.20	48.04
000.00	131462.85	54692.25	76770.60	26108.24	5066.24	31174.48	87
000.00	78011.84	38687.35	39324.49	11129.80	2819.47	13949.27	16.89
000.00	1149937.18	239229.30	910707.52	328166.22	58046.12	386212.44	
285.71	164276.74	34174.70	130101.07	46880.88	8292.30	55173.20	86.35

[fol. 96] "EXHIBIT I"

(Copy)

April 21, 1922.

Colector of Internal Revenue, Dallas, Texas.

SIR: Herewith we hand you on behalf of Burk-Waggoner Oil Association of Wichita Falls, Texas, a Claim for Refund of 1919 Excess Profits Taxes in the sum of $409,774.03, which you will please file.

Will you kindly acknowledge receipt of this, giving us the date it reached your office.

Very truly yours, (Signed) Harry C. Weeks. HCW-e.

[fol. 97] "EXHIBIT J"

(Copy)

Treasury Department, Internal Revenue Service, Dallas, Texas

April 25, 1922.

Burk-Waggoner Oil Association, c/o Weeks, Morros & Francis, Wichita Falls, Texas.

SIRS: Receipt is acknowledged of the following claims, filed in this office under date of April 24, 1922:

Claim for Abatement, $—.
Claim for Refund, $409,774.03.
Claim for Credit, —.

The above will receive further consideration, and will be forwarded to the Commissioner, Internal Revenue, Washington, D. C., for final disposition.

Respectfully, Geo. C. Hopkins, Collector. jgh. FHS.MM.

[fol. 98] In addition to the stipulation the testimony of CLOIS L. GREENE, witness for plaintiff, was taken as follows, to-wit:

"CLOIS L. GREENE, witness for plaintiff, being first duly sworn, examined in chief by Mr. Weeks, testified as follows:

Q. What is your name?
A. Clois L. Greene.
Q. Where do you live?
A. Wichita Falls, Texas.
Q. Where did you live in 1919?
A. Wichita Falls, Texas.
Q. Were you connected in any way with the enterprise known as the Burk-Waggoner Oil Association?

A. I was Secretary and Treasurer.

Q. Did you also own an interest in that?

A. Yes, sir.

Q. What percentage of the total outstanding interest in the Burk-Waggoner Oil Association did you own in the year 1919?

A. I owned 55 shares out of 600 shares.

Q. Do you know what percentage that is?

A. I believe it is a little over 9 per cent.

[fol. 99] Q. Do you know the amount of taxes that the Burk-Waggoner Oil Association paid?

A. Yes, sir.

Q. What was that amount?

A. Something around $560,000.00.

Q. Have you calculated the percentage of that, which is attributable to you or to your ownership of interest?

A. I believe I have. The percent I held would show my part of that tax $51,413.00.

Q. Did you file a tax return, individual tax return, for the year 1919?

A. Yes, sir.

Q. What net income did that show?

A. I had a loss in 1919.

Q. What was the amount of that loss?

A. It was $41,958.00.

Q. Mr. Greene, can you state to the Court why the Burk-Waggoner Oil Association filed the sort of tax report that it did file?

A. I would like to go into detail a little on that.

Q. All right sir.

A. We organized and started this company in September, this partnership, September, 1918. Operating during the 4 months of that year, and the first four months of 1919. A group of individuals with the understanding in my mind all the time that we were operating as partners, as a partnership. I never understood or knew that we were liable for the corporation tax until after we contracted to sell our property.

Q. When was that?

[fol. 100] A. It was May 5th, 1919.

Q. Is the sale of that property the source from which this profit was derived?

A. Yes, sir, that is the only property that we owned.

Q. What happened after you had made this contract of sale?

A. This property was sold to A. D. Morton, who represented the Ryan Petroleum Company. Mr. Morton had his attorney in Wichita Falls, Mr. Roland, this trade was closed in the office of Carrigan, Brittain & Mortgomery, of Wichita Falls, a day or so after we had agreed on a sale, which in their office, I came in touch with some revenue officer down in the office, and he brought up the point, that we would be liable for a corporation tax, that this company we had was the same as a corporation. That was the first intimation I had ever had of such, because the previous week, the minute that I knew we had this company sold I had been buying stock in it on the

board, as high as $2,950.00 per share, never dreaming that I had a tax to pay on it only as an individual, we calculated on splitting among our stockholders the total sum.

Mr. Deibert: At this time I want to call attention to the pleadings here, the pleadings are that the Burk-Waggoner Oil Association is the tax payer and paid the tax. Mr. Greene is not a party to this suit. He is not named in the pleadings as one of the alleged partners; nor is anybody named in these pleadings here as the alleged partners in this proceeding, the suit being alone by the Burk-Waggoner Oil Association, and no attempt, if it is a partnership, to give the name of the partners. I doubt if the testimony, particularly that part of it which he states that his understanding was that it was a partnership, is admissible. A partnership must be some sort of an agreement among several partners, they ought to have been made a party to this suit, to determine anything about it.

[fol. 101] The Court: Yes, I would not strike the testimony, of course, but the suggestions may become interesting later on. However, if counsel wants to amend and put in Greene and these others, as partners, trading under the name of the Burk-Waggoner Company, I would allow that amendment, if they think it is material.

Mr. Weeks: At this time I don't think it is material, we think, that for the purpose of litigation in this State, that we have such an enterprise that can sue in the name of the enterprise.

The Court: Do your pleadings set out how many partners there are?

Mr. Weeks: No, sir.

The Court: Merely the stipulation shows that?

Mr. Weeks: No, sir, I don't think the stipulation shows the number of prople interested. It certainly leads to the conclusion that there were a good many interested in the enterprise.

The Court: At the present time I overrule the motion of counsel to strike the testimony, and give him an exception.

Cross-examination.

By Mr. Deibert:

Q. What was your purpose in organization of the Burk-Waggoner Oil Association, as an association instead of a partnership?

A. We began this company with 14 men, two of whom dropped out after 40 days. At that time the Burkburnett field, it was customary to issue shares of interest or stock certificates, to give people something to show for their money, it was a new business to me, I went down in the rush, like everyone else, and started me a little company, got a lease and wanted to sell stock in it, or interest. I operated from September 6th to November 15th, before—I did not [fol. 102] know what I was doing, I was just trying to sell interest, and stock, and it came to my knowledge that I had to file some kind of a paper in the County records before I could issue these certificates of interest and stock.

Q. Why did you adopt that form of organization, why didn't you adopt the usual partnership form of agreement?

A. I did not know anything about it. I went to this firm of lawyers, Carrigan, Brittain & Carrigan and told them what I was doing, or trying to do, and they had a form there, it seemed that this was a customary form, they just drew it up and we accepted it.

Q. Was it the purpose of the organizers of this association to limit their liability as partners.

A. It was, in the beginning.

Q. Wasn't it all the way through?

A. It was not discussed later.

Q. Wasn't that the primary intention?

A. Our first meeting, September 4th, two days previous to the time we organized, it was discussed in Vernon. It was discussed we go into this thing. We had contracted to buy a lease from Mr. Waggoner for $20,000.00, 14 of us were going together and buy this lease and try to put down a well. At this meeting we agreed we were to pay $500.00 apiece, first payment; the following Monday we went to Burkburnett and put up our first payment and decided that we would try to sell some interest to stock to help us out in meeting the balance due on this lease.

Q. You incorporated in your articles of association an article that limited your liability so that you would not have the same liability as if it were a true partnership?

A. Not that I know of.

Q. You agreed that the shareholders, or stockholders, if stock should be sold, that they should have no liability for the debts of the association?

[fol. 103] A. Not to my knowledge.

Q. Well, that happens to be in the stipulation.

A. It may be, it may be in there—I am frank to tell you——

Q. In the stipulation—in the articles of association, which are a part of the stipulation. Now Mr. Greene, I hand you a certified photostatic copy of a paper which I wish you would identify, do you recognize that signature?

A. Yes, sir, that is my signature.

Q. That is your individual income tax return for the calendar year 1919, that is the return and the form on which you made it, is it not?

A. That looks familiar.

Q. That is your signature?

A. Yes, sir, that is my signature.

Q. In block "C" of that return, the block is headed, income from partnerships, person- service corporations and fiduciaries, in this tax return, in schedules attached and made a part thereof you show an income of $9,800.63, Waggoner & Greene, Wichita Falls, Texas?

A. Yes, sir, I remember that.

Q. Was that your only partnership income?

A. That was income from the Waggoner and Greene partnership.

Q. Didn't you have any income from the Burk-Waggoner Oil Association?

A. Yes, sir, I did.

Q. Why didn't you report that under that block income partnerships?

A. Well, I didn't make my report, never have, I am not familiar with it.

Q. You swore to it?

A. I leave that to my bookkeeper and to my attorney.

Q. You swore that this return and the accompany- schedules and statements were true to the best of your knowledge and belief, for the taxable period stated?

[fol. 104] A. That may be true.

Q. It was true at the time you made them?

A. To the best of my knowledge and belief, yes, sir.

Q. Why is it that you did not report the income from the Burk-Waggoner Oil Association in this return, if it was a partnership income?

A. I am frank to tell you, I do not know.

Q. You do not know?

A. No, sir, I didn't make my report.

Mr. Deibert: I put this in evidence, certified photostatic copy of Mr. Greene's return for the year 1919.

Redirect examination.

By Mr. Weeks:

Q. State whether or not it is a fact that your receipts from this enterprise were included in that 1919 return, under a different block than the one about which counsel has interrogated you?

A. Yes, sir, my report shows the income derived from the Burk-Waggoner property.

Q. State whether or not you were advised that that was the method which the Government required you to take?

A. Yes, sir, I was.

Recross-examination.

By Mr. Deibert:

Q. By whom were you advised?

A. Mr. Weeks made my return, through my bookkeeper.

Q. Mr. Weeks, the counsel here?

A. Yes, sir.

Q. Mr. Greene, was any of this stock actually sold to anybody outside of these 14 original organizers?

A. Yes, sir.

[fol. 105] Q. To how many persons?

A. In the neighborhood of 200.

Q. Was it transferred from one person to another after having been sold?

A. Some of it was, yes, sir.

Q. Very much of it?

A. Well——

Q. There were no restrictions on the transfer, was there?

A. No, sir, it was open to be transferred, it was transferrable.

Q. At that time, evidently, about 200 persons held stock in this organization?
A. Yes, sir.

Redirect examination.

By Mr. Weeks:

Q. Mr. Greene, were you well acquainted with most of the people who were interested in this enterprise?
A. I believe I was acquainted, personally, with 80 or 85 per cent of them.
Q. State whether or not there were a number of people who had one and two shares?
A. Majority of the stockholders were one and two share stockholders.
Q. Now, as to those people who had one and two shares; state whether or not there are any of them with whom you are sufficiently familiar to know and to be able to state that they did not receive from other sources income which would have been above their exemption of one and two thousand dollars, depending upon whether they were married.

Mr. Deibert: If your honor please, I object to that question, I don't think the witness could possible have such information.
[fol. 106] The Court: I sustain the objection, I do not see the relevency of it, even if he should have it.
Mr. Weeks: That is all the plaintiff's testimony.
The Court: Any testimony for the defendant?
Mr. Deibert: None, your Honor.

[Title omitted]

REPORTER'S CERTIFICATE

I, T. C. Irby, certify that I reported all of the proceedings had in the above styled and numbered cause, during the trial thereof. That I have transcribed said proceedings, being the question and answer testimony, of the witness Clois L. Green, and that the same is true and correct.
Witness my hand this 17th day of March, A. D. 1924.
T. C. Irby, Court Reporter."

ORDER SETTLING BILL OF EXCEPTIONS

Whereupon, both plaintiff and defendant rested and closed; and thereupon, after consideration and on or about the 27th day of February, 1924, the District Court entered and rendered a judgment in

favor of the defendant and denying plaintiff any relief, to all of which the plaintiff duly excepted and, upon motion duly made, an order was entered allowing sixty days from and after the adjournment of this term of Court for the filing of the Bill of Exceptions.

And now, in furtherance of justice and that right may be done the plaintiff, Burk-Waggoner Oil Association, the latter tenders and presents the foregoing as its Bill of Exceptions in this case to the [fol. 107] action of the Court, and prays that the same may be settled and allowed and signed and sealed by the Court and made a part of the record, and the same is accordingly done this 21 day of April, A. D. 1924.

Wm. H. Atwell, Judge Presiding.

We approve this Bill as prepared by plaintiff's counsel.
Henry Zweifel, Attorneys for Defendant.

[fol. 108] In United States District Court

Petition for Writ of Error—Filed April 19, 1924

Now comes the Burk-Waggoner Oil Association, plaintiff herein, and says that on the 27th day of February A. D. 1924, the District Court entered a judgment herein in favor of the defendant against this plaintiff, in which judgment and the proceedings had prior thereto in this cause, certain errors were committed to the prejudice of this plaintiff, all of which will in more detail appear from the assignment of error which is filed with this petition.

Wherefore, this plaintiff prays that writ of error issue in its behalf out of the Supreme Court of the United States for the correction of errors so complained of and that a transcript of the record, proceedings and papers of this case, duly authenticated, may be sent to the Supreme Court of the United States.

Harry C. Weeks, Jno. M. Sternhagen, Attorneys for plaintiff, Burk-Waggoner Oil Association.

[fol. 109] In United States District Court

Assignments of Error—Filed April 19, 1924

The Plaintiff, Burk-Waggoner Oil Association, in connection with its Petition for Writ of Error, makes the following Assignment of Errors, which it avers occurred upon the trial of this cause and were committed in the entry of the judgment herein, to-wit:

First

The Court erred in failing and refusing to enter a judgment in favor of the plaintiff and allowing the recovery of the moneys paid by plaintiff, which relief was refused upon the theory that plaintiff

is an association which comes within the definition of a corporation as defined by the Revenue Act of 1918 and is subject to the income and excess-profits taxes imposed upon corporations by the said Revenue Act of 1918.

Second

The Court erred in holding that the plaintiff was a corporation or association coming within the definition of a corporation contained in the Revenue Act of 1918 and subject to the taxes imposed by said Act upon corporations.

Third

The Court erred in failing and refusing to enter a judgment in favor of the plaintiff, and in failing and refusing to hold that the Burk-Waggoner Oil Association was a partnership within the terms of the Revenue Act of 1918.

Fourth

The Court erred in failing and refusing to enter judgment for plaintiff for the amount sued for, and in thereby giving effect to regulations adopted by the Commissioner of Internal Revenue with the approval and consent of the Secretary of the Treasury, which [fol. 110] regulations provide in substance that partnerships organized and created as the Burk-Waggoner Oil Association was organized and created are subject to the income and excess-profits taxes imposed by the Revenue Act of 1918 upon corporations, contrary to the terms and provisions of the said Revenue Act of 1918, because said regulations are contrary to law and constitute an attempt upon the part of the Executive Department of the Government to legislate in conflict with the terms and provisions of Article 1, Section 1, of the Constitution of the United States, and the Court erred in not holding that so much of said regulations, as undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such, was contrary to the said Article 1, Section 1, of the Constitution of the United States.

Fifth

The Revenue Act of 1918 which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to impose an income and excess-profits tax upon such partnership is contrary to the provisions of Article 1, Section 2, of the Constitution of the United States in that it imposes a direct tax not apportioned among the States and not imposed upon income, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such and to impose a tax thereon, is contrary to the said Article 1, Section 2, of the Constitution of the United States.

Sixth

The Revenue Act of 1918, which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to impose upon such partnership the income and excess-profits taxes imposed upon corpora-
[fol. 111] tions by said Act, is contrary to the provisions of Article 1, Section 8, of the Constitution of the United States in that it is not uniform and is discriminatory and arbitrary and the Court erred in not holding that the said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such, is contrary to the said Article 1, Section 8, of the Constitution of the United States.

Seventh

The Revenue Act of 1918 which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to subject it to the taxes imposed by said Act upon corporations, is contrary to the provisions of Article 1, Section 9, of the Constitution of the United States in that it imposes a direct tax not in proportion to any census or enumeration and not upon income, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and subject to the taxes imposed by said Act upon corporations, is contrary to the said Article 1, Section 9, of the Constitution of the United States.

Eighth

The Revenue Act of 1918, which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, to be a corporation and subject to the income and excess-profits taxes imposed by said Act upon corporations, is contrary to the provisions of the Sixteenth Amendment of the Constitution of the United States in that such a tax as applied to the Burk-Waggoner Oil Association is a direct tax not based upon income and not apportioned among the several States according to
[fol. 112] population, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and subject to the income and excess-profits taxes imposed therein upon corporations, is contrary to the Sixteenth Amendment of the Constitution of the United States.

Ninth

The Court erred in holding that the Burk-Waggoner Oil Association is an entity and an association coming within the definition of a corporation contained in the Revenue Act of 1918, and in not holding that the individual partners in the Burk-Waggoner Oil Association

are each subject to taxation upon their distributive share of the profits of said partnership and that said association or partnership is not liable for the income and excess-profits taxes imposed upon corporations by the said Revenue Act of 1918.

Tenth

The Court erred in entering judgment in favor of the defendant and denying plaintiff any relief.

Eleventh

The holding of the Court that the tax paid by the Burk-Waggoner Oil Association was authorized by the Revenue Act of 1918 is erroneous in that if such Act be given such construction the same is unconstitutional and contrary to the Fifth Amendment of the Constitution of the United States because such a construction imposes upon the Burk-Waggoner Oil Association and its individual members a tax in varying amounts irrespective of their income and wholly arbitrary and irrespective of the rate of tax in excess of such rates and upon persons who, by the terms of said Revenue Act of 1918, are not subject to income and excess-profits taxes for the year involved, all of which would be unlawful and unconstitutional.

Twelfth

[fol. 113] The holding of the Court that the tax paid by the Burk-Waggoner Oil Association was authorized by the Revenue Act of 1918 is erroneous in that if such Act be given such construction the same is unconstitutional, and contrary to Article 1, Section 8, and Article 1, Section 9, of the Constitution of the United States and of the Sixteenth Amendment to the Constitution of the United States, in that it imposes a direct tax not upon income but irrespective of income and same is not apportioned among the several States or upon the basis of such or upon any census or enumeration, and is levied irrespective of the amount of income received and at rates greater than provided for by the Revenue Act of 1918, all of which would be unlawful and unconstitutional.

Wherefore, plaintiff prays that said judgment be reversed.
Harry C. Weeks, John M. Sternhagen, Attorneys for Plaintiff.

[fol. 114] In United States District Court

Order Allowing Writ of Error—Filed April 21, 1924

On this the 21 day of April, 1924, comes the plaintiff, by its attorneys, and files herein and presents to the Court its petition praying for the allowance of writ of error and an assignment of errors

intended to be urged by it; praying also that a transcript of the record, proceedings and papers upon which the judgment herein was rendered, duly authenticated, may be sent to the Supreme Court of the United States, and that such other and further proceedings may be had as are proper in the premises.

In consideration whereof the Court does allow the writ of error upon the plaintiff being bound, according to law, in the sum of One Thousand ($1,000.00) Dollars.

Wm. H. Atwell, U. S. District Judge, Presiding.

[fols. 115 & 116] Bond on Writ of Error for $1,000—Approved; omitted in printing

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[fol. 117] In United States District Court

Writ of Error—Filed April 21, 1924

The President of the United States to the Honorable the Judge of the District Court of the United States for the Northern District of Texas, Greeting:

Because in the record and proceedings, as also in the rendition of the judgment of a plea which is in the said District Court, before you, or some of you, between Burk-Waggoner Oil Association, plaintiff in error, and George C. Hopkins, Collector of Internal Revenue, Second District of Texas, defendant in error, a manifest error hath happened, to the great damage of the said Burk-Waggoner Oil Association, plaintiff in error, as by its complaint appears. We being willing that error if any hath been, should be duly corrected, and full and speedy justice done to the parties aforesaid in his behalf, do command you, if judgment be therein given, that then under your seal, distinctly and openly you send the record and proceedings aforesaid with all things concerning the same, to the Supreme Court of the United States, together with this writ, so that you have the same at Washington, D. C., in not exceeding thirty days from 21st day of April 1924 being the date of issuance of the citation herein, in the United States Circuit Court of Appeals, to be then and there held, that the record and proceedings aforesaid being inspected, the said United States Circuit Court of Appeals may cause further to be done therein to correct that error, what of right, and according to the laws and customs of the United States, should be done.

Witness the Honorable William Howard Taft, Chief Justice of the United States, the 21 day of April, in the year of our Lord, one thousand nine hundred and twenty-four.

Louis C. Maynard, Clerk of the District Court of the United States for the Northern District of Texas, by —— ——, Deputy. (The seal of the U. S. District Court, Northern Dist. Texas, Dallas.)

Allowed by Wm. H. Atwell, United States District Judge.

[File endorsement omitted.]

[fol. 118] IN UNITED STATES DISTRICT COURT

PRÆCIPE FOR TRANSCRIPT OF RECORD—Filed May 1st, 1924

To the Clerk of the above entitled court:

You will please prepare transcript of the record in this cause to be filed in the office of the Clerk of the Supreme Court of the United States under the writ of error heretofore allowed by this court, and include in said transcript the following pleadings, proceedings and papers on file, to-wit:

Plaintiff's Second Amended Original Petition;
Defendant's Answer;
Opinion of the Court;
Judgment;
Motion for enlargement of time to prepare and file Bill of Exceptions;
Order allowing additional time for preparing Bill of Exceptions;
Bill of Exceptions;
Petition for Writ of Error;
Assignment of Errors;
Order allowing Writ of Error and fixing Appeal Bond;
Appeal Bond;
Clerk's Certificate of transcript of record;
Writ of Error;
Clerk's return to writ of error;
Præcipe for transcript of record;
Citation;

said transcript to be prepared as required by law and the rules of the Supreme Court of the United States.

Harry C. Weeks, Jno. M. Sternhagen, Attorneys for Plaintiff, Burk-Waggoner Oil Assn.

[fol. 119] Receipt is hereby acknowledged of the delivery of a copy of the foregoing Præcipe to the undersigned attorney of record for the defendant in said cause.

Henry Zweifel, U. S. District Attorney

[fol. 120] CITATION—In usual form, showing service on Geo. C. Hopkins; filed April 21, 1914; omitted in printing

[fol. 121] IN UNITED STATES DISTRICT COURT

CLERK'S CERTIFICATE

I, Louis C. Maynard, Clerk of the United States District Court for the Northern District of Texas, do hereby certify that the foregoing is a true and correct transcript of the record, assignments of error and all proceedings in Cause No. 3301, Law, Wherein Burk-Waggoner Oil Association is plaintiff, and Geo. C. Hopkins, Collector of Internal Revenue is Defendant, as fully as the same now remain on file and of record in my office at Dallas, Texas, save and except that the Original Writ of Error and Citation in Error are included therein in place of copies of same.

Witness my hand officially and the seal of said Court at Dallas, Texas, this — day of May, A. D. 1924.

Louis C. Maynard, Clerk U. S. District Court, Northern District of Texas, at Dallas, by Mary Conger, Deputy. (The Seal of the U. S. District Court, Northern Dist. Texas, Dallas.)

Endorsed on cover: File No. 30,353. N. Texas D. C. U. S. Term No. 397. Burk-Waggoner Oil Association, plaintiff in error, vs. George C. Hopkins, collector of internal revenue, second district of Texas. Filed May 20th, 1924. File No. 30,353.

Office Supreme Court,
FILED
SEP 23 1924
WM. R. STANSBURY
CLERK

IN THE

Supreme Court of the United States.

OCTOBER TERM, A. D. 1924.

No. 397 67

BURK-WAGGONER OIL ASSOCIATION,
Plaintiff in Error,

vs.

GEORGE C. HOPKINS, COLLECTOR OF INTERNAL REVENUE,
SECOND DISTRICT OF TEXAS,
Defendant in Error.

IN ERROR TO THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF TEXAS.

BRIEF FOR PLAINTIFF IN ERROR.

HARRY C. WEEKS,
ARNOLD R. BAAR,
Attorneys for Plaintiff in Error.

WEEKS, MORROW, FRANCIS & HANKERSON,
Staley Building,
Wichita Falls, Texas.
KIXMILLER & BAAR,
Illinois Merchants Bank Bldg.,
Chicago, Illinois,
Of Counsel.

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IN THE

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No. 397

BURK-WAGGONER OIL ASSOCIATION,
Plaintiff in Error,

vs.

GEORGE C. HOPKINS, COLLECTOR OF INTERNAL REVENUE, SECOND DISTRICT OF TEXAS,
Defendant in Error.

IN ERROR TO THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF TEXAS.

BRIEF FOR PLAINTIFF IN ERROR.

STATEMENT OF THE CASE.

The plaintiff below has brought this case directly to this court to review by writ of error the adverse decision of the District Court of the United States for the Northern District of Texas. The plaintiff in error, hereafter referred to as plaintiff, is the Burk-Waggoner Oil Association, alleged to be an "unincorporated association or partnership." The defendant in error is the Collector of Internal Revenue for the Second District of Texas. The suit was brought to recover $145,827.67 paid as income and excess-profits taxes and interest thereon by the

Burk-Waggoner Oil Association for the year 1919 under the Revenue Act of 1918. The trial below was without a jury. The judgment of the Court below denied plaintiff any relief whatsoever. (R.* p. 12) The Court's opinion is set forth in the Record, pages 4 to 12, and is reported in 296 Fed. 492.

Two principal questions are presented:

1. **Does the Revenue Act of 1918, when properly construed, impose any income and profits tax upon plaintiff, as if incorporated; or does the statute require that the income from the enterprise be taxed only to the members individually, as in other partnerships?**

2. **If the Revenue Act of 1918 requires that the plaintiff pay corporate income and excess-profits taxes, does this result in unconstitutional taxation?**

The plaintiff contends that it is a partnership and should be treated as such for income tax purposes and that the collection of corporate income and excess-profits taxes from it, if not contrary to the statute, was unconstitutional.

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* Reference are to the printed record.

THE FACTS.

Most of the facts presented were stipulated, and there is no dispute on the facts. By the stipulation it was agreed that the Burk-Waggoner Oil Association was organized on October 15, 1918, by the private agreement of six individuals residing in Texas, and all of its operations were conducted in that State. The purpose of the enterprise was to engage in all branches of the oil business. By the agreement between the organizers, called the articles of association, the name "Burk-Waggoner Oil Association" was adopted; the capital was fixed at $60,000.00, and divided into transferable shares. The enterprise was styled an "unincorporated joint-stock association" and the term of its existence fixed for the life of the last surviving organizer, and twenty-one years thereafter, unless sooner dissolved. (R. p. 15) The management of the enterprise was vested in a Board of Trustees to be elected annually after the first year, the organizers constituting the Board for the first year. General powers of management were given the trustees; they were authorized to sue in their own names or in the name of the Burk-Waggoner Oil Association and to take the title to the property of the enterprise in their names as trustees, holding as joint tenants under the trusts provided for. The owners of shares were to have no legal right to the property held by the trustees and no right to call for the partition or dissolution of the enterprise, nor was the death or bankruptcy of a member or the transfer of his interest to dissolve it. Shares were to be considered personal property and were to entitle the holder to a division of the principal and profits in due proportion to the number of shares held. (R. pp. 17, 18)

The trustees were prohibited from binding the shareholders personally on any engagement which they might make and the property of the enterprise was charged with primary liability for all obligations incurred. (R. p. 19) Ultimate control was vested in the shareholders through their right to elect trustees annually, the right of the holders of one-fourth of the shares to call special meetings at any time and the provision in Article 14, (R. p. 21) that *"The members of the Board of Trustees shall at all times be subject to the orders of the shareholders, who may at any time and for any cause by vote of a majority of all of the shares then issued and outstanding remove any one or all of them from office and devolve upon other members the duties and functions of the office."* The articles could be amended by a vote of three-fourths of the shares represented at a meeting at which a quorum was present. (R. pp. 19, 21)

Of the capital stock, $40,000 was to be paid in by transferring to the Trustees an oil and gas lease owned by the organizers on sixty acres of land in Wichita County, Texas. The balance of the capital stock was to be sold for cash. (R. pp. 21, 22.) The enterprise could be dissolved by a vote of the holders of three-fourths of the stock issued and outstanding. (R. p. 22)

A declaration of trust was executed by the trustees who acknowledged that they would hold all property coming to them by virtue of their office upon the trusts and conditions contained in the articles of association. (R. p. 23) The articles and the declaration of trust were recorded in Wichita County, Texas.

The oil and gas lease referred to was assigned to the trustees on December 14, 1918. (R. p. 25) With funds raised from the sale of the remaining capital stock, an oil well was drilled upon this property, which was completed on or about April 25, 1919, as a very productive

well. It caused a large enhancement in the value of the property, and the whole property was sold on May 5, 1919, for $2,000,000. A profit of $24,564.96 was received from the production of oil prior to the sale and a profit of $1,813,488.94 from the sale of the property. (See copy of tax return between pages 30 and 31, Record.)

After the sale no business was conducted except that incidental to winding up the concern's affairs. (R. p. 27) Those in charge of the enterprise learned that the Bureau of Internal Revenue considered concerns like the Burk-Waggoner Oil Association taxable under the Revenue Act of 1918 as if incorporated and required corporate tax returns from them. In accordance with this a corporate income and profits tax return was filed, showing a tax liability of $552,602.02, which was paid. One-fourth of the amount and some interest thereon, totaling $145,827.67 was paid to the defendant on March 28, 1922. (R. p. 27) Two claims for refund were filed; one was never passed upon and the other was rejected. (R. p. 27)

At the time the return was made there was in force and effect regulations adopted by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury, requiring all enterprises similar to the Burk-Waggoner Oil Association to make returns substantially in accordance with that made by it and to pay income and profits taxes thereon. Substantial penalties would have been asserted if the return had not been made or the tax paid. (R. pp. 27, 28)

There is contained in the stipulation various claims, corrected returns and correspondence relative to the tax liability of the enterprise, which are not pertinent to the present suit and need not be considered further than to state that the plaintiff in error endeavored unavailingly

to secure various reductions in tax liability upon several different theories.

The above facts are set forth in the stipulation, and, in addition thereto, one witness, Clois L. Greene, testified. His testimony was that he was one of the original organizers of the enterprise, was its Secretary and Treasurer and in 1919 owned 55 out of the 600 outstanding shares, and that the percentage of the tax paid proportionate to his interest amounted to $51,413. (R. pp. 49, 50) He also testified that he had no net income in 1919 but suffered a loss of $41,958. He filed an individual income tax return for that year showing that loss. In that return he reported all of the money which he had received from the Burk-Waggoner Oil Association; but he did not include in his return, under the division thereof for reporting partnership income, his distributive share of the profits of the concern, as he was advised that he was required by the Bureau of Internal Revenue to make his return otherwise. He also testified that he had paid as high as $2,950 per share for stock and that he considered the enterprise as a partnership, and that he had no intimation that it would be liable for corporate income taxes until after the sale above referred to was made. (R. pp. 50, 51, 52) The tax return of plaintiff shows that $1,250,000 was distributed in 1919. (R. p. 34, "Statement under Schedule L.")

PLEADINGS.

The trial was had upon plaintiff's second amended original petition in which the organization of the enterprise, the history of the business, the making of the tax returns, and the payment of the taxes were pleaded substantially as set forth above. (R. pp. 1, 2) It was alleged in this petition that the plaintiff in error was an "unincorporated association or partnership"; that it had no rights or charter granted by the laws of any state; that no taxes whatsoever should have been collected from it because (1) it was a partnership; (2) if it was subject to the corporate income and profits taxes contained in the Revenue Act of 1918, that Act was unconstitutional because contrary to Article 1, Sections 1, 2, 8 and 9 of the Constitution and the Fifth and Sixteenth Amendments thereto. (R. p. 3) Judgment was sought for the tax and interest paid defendant in error.

The pleadings of the defendant consisted of a general demurrer, and a general denial. (R. pp. 3, 4)

JUDGMENT AND APPEAL.

Upon these pleadings and facts the Court returned a judgment denying plaintiff any relief. Plaintiff excepted to the judgment of the Court and in due course its bill of exceptions was allowed (R. pp. 54 and 55), and a petition for writ of error sued out to this court.

SPECIFICATION OF ERRORS.

The following specifications show the errors relied upon:

1. The Court below erred in holding that the Burk-Waggoner Oil Association was taxable as a corporation under the Revenue Act of 1918, and in not holding that the income from the enterprise should be taxed only to the members thereof separately. (Assignments of Error Nos. 1, 2, 3, 9 and 10; set out below and at Record pp. 55, 56, 57, 58.)

2. The Court below erred in not holding that so much of the Revenue Act of 1918 as sought to impose an income and excess profits tax upon the Burk-Waggoner Oil Association was unconstitutional because the tax so levied was a direct property tax not imposed upon income and not apportioned among the several states, and therefore violated Sections 2 and 9 of Article I of the Constitution. (Assignments of Error Nos. 5, 7 and 12; below, and Record pp. 56, 57, 58.)

3. The Court below erred in not holding that the Revenue Act of 1918 was unconstitutional because the income and excess profits tax imposed by it upon the plaintiff's members and collected from the plaintiff, was imposed at rates wholly arbitrary and in excess of the rates provided by law for individuals and irespective of whether or not such persons had received income for the year involved; and the act therefore, violated Sections 2 and 9 of Article I and the Fifth Amendment to the Constitution. (Assignment of Error No. 11, Record, p. 58.)

The Assignments of Error are for convenience here reprinted in full:

ASSIGNMENTS OF ERROR.

Twelve errors were assigned, which are set forth in the Record, pages 55 to 58, and are as follows:

First.

The Court erred in failing and refusing to enter a judgment in favor of the plaintiff and allowing the recovery of the moneys paid by plaintiff, which relief was refused upon the theory that plaintiff is an association which comes within the definition of a corporation as defined by the Revenue Act of 1918 and is subject to the income and excess profits taxes imposed upon corporations by the said Revenue Act of 1918.

Second.

The Court erred in holding that the plaintiff was a corporation or association coming within the definition of a corporation contained in the Revenue Act of 1918 and subject to the taxes imposed by said Act upon corporations.

Third.

The Court erred in failing and refusing to enter a judgment in favor of the plaintiff, and in failing and refusing to hold that the Burk-Waggoner Oil Association was a partnership within the terms of the Revenue Act of 1918.

Fourth.

The Court erred in failing and refusing to enter judgment for the plaintiff for the amount sued for, and in thereby giving effect to the regulations adopted by the Commissioner of Internal Revenue with the approval and consent of the Secretary of the Treasury, which regulations provide in substance that partnerships organized and created as the Burk-Waggoner Oil Association was organized and created are subject to the income and excess-profits taxes imposed by the Revenue Act of 1918 upon corporations, contrary to the terms and provisions of the

said Revenue Act of 1918, because said regulations are contrary to law and constitute an attempt upon the part of the Executive Department of the Government to legislate in conflict with the terms and provisions of Article 1, Section 1, of the Constitution of the United States, and the Court erred in not holding that so much of said regulations, as undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such, was contrary to said Article 1, Section 1, of the Constitution of the United States.

Fifth.

The Revenue Act of 1918 which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to impose an income and excess-profits tax upon such partnership is contrary to the provisions of Article 1, Section 2, of the Constitution of the United States in that it imposes a direct tax not apportioned among the States and not imposed upon income, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such and to impose a tax thereon, is contrary to the said Article 1, Section 2, of the Constitution of the United States.

Sixth.

The Revenue Act of 1918, which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to impose upon such partnership the income and excess-profits taxes imposed upon corporations by said Act, is contrary to the provisions of Article 1, Section 8, of the Constitution of the United States in that it is not uniform and is discriminatory and arbitrary and the Court erred in not holding that the said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and taxable as such, is contrary to the said Article 1, Section 8, of the Constitution of the United States.

Seventh.

The Revenue Act of 1918 which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, as a corporation and to subject it to the taxes imposed by said Act upon corporations, is contrary to the provisions of Article 1, Section 9, of the Constitution of the United States in that it imposes a direct tax not in proportion to any census or enumeration and not upon income, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and subject to the taxes imposed by said Act upon corporations, is contrary to the said Article 1, Section 9, of the Constitution of the United States.

Eighth.

The Revenue Act of 1918, which undertakes to classify a partnership organized as was the Burk-Waggoner Oil Association, as shown by the evidence in this case, to be a corporation and subject to the income and excess-profits taxes imposed by said Act upon corporations, is contrary to the provisions of the Sixteenth Amendment of the United States in that such a tax as applied to the Burk-Waggoner Oil Association is a direct tax not based upon income and not apportioned among the several States according to population, and the Court erred in not holding that said Revenue Act of 1918, wherein it undertook to classify the Burk-Waggoner Oil Association as an entity or corporation and subject to the income and excess-profits taxes imposed therein upon corporations, is contrary to the Sixteenth Amendment of the Constitution of the United States.

Ninth.

The Court erred in holding that the Burk-Waggoner Oil Association is an entity and an association coming within the definition of a corporation contained in the Revenue Act of 1918, and in not holding that the individual partners in the Burk-Waggoner Oil Association are each subject to taxa-

tion upon their distributive share of the profits of said partnership and that said association or partnership is not liable for the income and excess-profits taxes imposed upon corporations by the said Revenue Act of 1918.

Tenth.

The Court erred in entering judgment in favor of the defendant and denying plaintiff any relief.

Eleventh.

The holding of the Court that the tax paid by the Burk-Waggoner Oil Association was authorized by the Revenue Act of 1918 is erroneous in that if such Act be given such construction the same is unconstitutional and contrary to the Fifth Amendment of the Constitution of the United States because such a construction imposes upon the Burk-Waggoner Oil Association and its individual members a tax in varying amounts irrespective of their income and wholly arbitrary and irrespective of the rate of tax in excess of such rates and upon persons who, by the terms of said Revenue Act of 1918, are not subject to income and excess-profits taxes for the year involved, all of which would be unlawful and unconstitutional.

Twelfth.

The holding of the Court that the tax paid by the Burk-Waggoner Oil Association was authorized by the Revenue Act of 1918 is erroneous in that if such Act be given such construction the same is unconstitutional, and contrary to Article 1, Section 8, and Article 1, Section 9, of the Constitution of the United States and of the Sixteenth Amendment to the Constitution of the United States, in that it imposes a direct tax not upon income but irrespective of income and same is not apportioned among the several States or upon the basis of such or upon any census or enumeration, and is levied irrespective of the amount of income received and at rates greater than provided for by the Revenue Act of 1918, all of which would be unlawful and unconstitutional.

STATUTES INVOLVED.

"THE REVENUE ACT OF 1918."

TITLE I. GENERAL DEFINITIONS.

SEC. 1 (40 Stat. 1057). That when used in this Act—
* * *

The term "corporation" includes associations, joint-stock companies, and insurance companies; * * *

TITLE II. INCOME TAX.

* * * *Part II. Individuals.*

SEC. 210 (40 Stat. 1062). That * * * there shall be levied, collected and paid for each taxable year upon the net income of every individual a normal tax at the following rates: * * *

SEC. 211 (40 Stat. 1062). That * * * in addition to the normal tax imposed by Sec. 210 of this Act, there shall be levied, collected, and paid for each taxable year upon the net income of every individual, a surtax equal to the sum of the following: * * *

SEC. 212 (40 Stat. 1064). That in the case of an individual, the term "net income" means the gross income as defined by Sec. 213, less the deductions allowed by Sec. 214. * * *

SEC. 213 (40 Stat. 1065). That for the purposes of this title (except as otherwise provided in Sec. 233) the term "gross income"—

(a) Includes * * * gains or profits or income derived from any source whatever. * * *

SEC. 218 (40 Stat. 1070). (a) That individuals carrying on business in partnership shall be liable for income

tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year. * * *

* * * *Part III. Corporations.*

SEC. 230 (40 Stat. 1075). (a) That * * * there shall be levied, collected, and paid for each taxable year upon the net income of every corporation a tax at the following rates: * * *

TITLE III. WAR-PROFITS AND EXCESS-PROFITS TAX.

* * * *Part II. Imposition of Tax.*

SEC. 301 (40 Stat. 1088). * * *

(b) For the taxable year 1919 and each taxable year thereafter there shall be levied, collected and paid upon the net income of every corporation (except corporations taxable under subdivision (c) of this section) a tax equal to the sum of the following: * * *

Part VII. Miscellaneous.

SEC. 335 (40 Stat. 1095). * * *

Any tax paid by a partnership or personal service corporation for any period beginning on or after January 1, 1918, shall be immediately refunded to the partnership or corporation as a tax erroneously or illegally collected.

TITLE XIII. GENERAL ADMINISTRATIVE PROVISIONS.

SEC. 1309 (40 Stat. 1143). The Commissioner, with the approval of the Secretary, is hereby authorized to make all needful rules and regulations for the enforcement of the provisions of this Act. * * *

GENERAL LAWS OF THE STATE OF TEXAS, 1907, PASSED AT THE REGULAR SESSION OF THE THIRTEENTH LEGISLATURE.

* * * * *

Unincorporated Joint Stock Companies—Permitting Suit in Company Name.

S. B. NO. 239. CHAPTER CXXVIII.

(Vernon's Sayles' Revised Civil Statutes of Texas, 1914, title 102, Chap. 2, Arts. 6149-6154.)

"An Act to authorize unincorporated joint stock companies or associations to sue and be sued in their company or distinguishing name, and to prescribe the mode and effect of service on such unincorporated companies, and the legal effect of judgments that shall be rendered in such actions, and declaring an emergency.

Be It Enacted by the Legislature of the State of Texas:

[ART. 6149] SECTION 1. That hereafter any unincorporated joint stock company or association, whether foreign or domestic, doing business in this State, may sue or be sued in any court of this State, having jurisdiction of the subject matter, in its company or distinguishing name; and it shall not be necessary to make the individual stockholders or members thereof parties to the suit.

[ART. 6150] SECTION 2. In suits against unincorporated joint stock companies or associations, service of citation may be had on the president, secretary, treasurer or general agent of such unincorporated companies.

[ART. 6151] SECTION 3. In suits by or against such unincorporated companies, whatever judgment shall be rendered, shall be as conclusive on the individual stockholders and members thereof as if they were individually parties to such suits.

[ART. 6152] SECTION 4. Where suit shall be brought against an unincorporated joint stock company or association and the only service had, shall be upon the president, secretary, treasurer or general agent of such company or association, and judgment shall be rendered

against the defendant company, such judgment shall be binding on the joint property of all the stockholders or members thereof, and may be enforced by execution against the joint property, but such judgment shall not be binding on the individual property of the stockholders or members, nor authorize execution against it.

[Art. 6153] Section 5. In a suit against an unincorporated joint stock company or association, in addition to service on the president, secretary, treasurer or general agent of such companies or associations, service of citation may also be had on any or all of the stockholders or members of such companies or associations, and in the event judgment shall be against such unincorporated company or association, it shall be equally binding upon the individual property of the stockholders or members so served, and executions may issue against the property of the individual stockholders or members, as well as against the joint property; but executions shall not issue against the individual property of the stockholders or members until execution against the joint property has been returned without satisfaction.

[Art. 6154] Section 6. This act shall not affect nor impair the right now allowed unincorporated joint stock companies and associations to sue in the individual names of the stockholders or members, nor the right of any person to sue the individual stockholders or members; but the provisions of this act shall be construed as cumulative merely of other remedies now existing under the law.

— — Section 7. The fact that there is now no adequate law upon this subject, and thereby causing loss to many citizens of this State, creates an imperative public necessity that the constitutional rule requiring bills to be read on three several days be suspended and that this act shall take effect from and after its passage, and it is so enacted.

Approved April 18, 1907.

Takes effect ninety days after adjournment."

BRIEF OF ARGUMENT.

POINTS AND AUTHORITIES.

I.

The Revenue Act of 1918, when properly construed, does not impose an income or profits tax upon the Burk-Waggoner Oil Association, but the income from the enterprise was taxable only to its individual members as the income from a partnership.

1. The Burk-Waggoner Oil Association is a partnership.

Thompson v. *Schmitt,* 114 Tex. ....., (decided by the Supreme Court of Texas, June 24, 1925).

Victor Ref. Co. v. *City Nat'l Bank of Commerce, et al.,* 114 Tex. ....., (decided by the Supreme Court of Texas, June 24, 1925).

Edwards v. *Old Settlers Association,* (Tex. Civ. App.), 166 S. W. 423, 426.

Clark v. *Brown,* (Tex. Civ. App.), 108 S. W. 421, 433.

Meehan v. *Valentine,* 145 U. S. 611, 618, 623.

Merchants Nat'l Bank v. *Wehrmann,* 202 U. S. 295, 300.

Bates, Law of Partnership, Vol. 1, pars. 72, 160-163.

20 Ruling Case Law, p. 887, Partnerships, par. 98.

Winship v. *Bank of U. S.,* 5 Peters 529.

Irwin v. *Williar,* 110 U. S. 499.

2. The Revenue Act of 1918 expressly provides that the members of all partnerships are taxable upon their distributive shares of the partnership income, whether distributed or not, and excludes all partnerships from liability for income and profits taxes.

Revenue Act of 1918, Act of February 24, 1919, (c. 18, 40 Stat. 1057);
Title II, Secs. 210, 211, 218 (a), 224, 230, (40 Stat. 1062, 1070, 1074, 1075).
Title III, Secs. 301, 335 (c) (40 Stat. 1088, 1095).

Revenue Act of 1917, Act of Oct. 3, 1917, Sec. 201 (c. 63, 40 Stat. 300, 303).

3. In view of the conflict between the specific provisions of the Revenue Act of 1918, for the taxation of partnership income to the members only, and the definition of the term "corporation", one or the other must be limited; the settled rules of statutory construction require that the limitation be so applied that no partnership income should be subjected to the taxes imposed upon corporations.

Revenue Act of 1918, Act of February 24, 1919, (c. 18, 40 Stat. 1057);
Title 1, Sec. 1 (40 Stat. 1057).
Title II, Sec. 213, 218 (40 Stat. 1065, 1070).

(a) A specific provision in a statute controls over a general provision.

United States v. *Chase*, 135 U. S. 255, 260.
Chew Hing Lung v. *Wise*, 176 U. S. 156, 160.
American Net and Twine Company v. *Worthington*, 141 U. S. 468, 474.

(b) A construction will be adopted which will give every word of the statute a meaning without disregarding any other word or provision in it.

Sarlls v. *United States*, 152 U. S. 570.
Mercantile Bank v. *New York*, 121 U. S. 138.
Washington Market Co. v. *Hoffman*, 101 U. S. 112.
Pennsylvania, Statutes (1920), Arts. 16656-16684.
New Jersey, Compiled Statutes, Sec. 30.
Virginia, Pollard's Code, 1904, Sec. 2878.
Ohio, Pages Rev. Gen. Code, Vol. II, Sec. 8059.
Rouse v. *Detroit*, 111 Mich. 251, 69 N. W. 511.
Staver v. *Blake*, 111 Mich. 282, 69 N. W. 508.
Goodspeed v. *Hally*, 199 Mich. 273, 165 N. W. 943.
First Nat'l Bank v. *Vanden Brooks*, 206 Mich. 177; 172 N. W. 582.
Chicago Title & Trust Co. v. *Smietanka*, 275 Fed. 60.
M. & M. Lloyds Ins. Exchange v. *Southern Trading Co.* (Tex. Civ. App.), 205 S. W. 352.
Crow v. *Cattlemen's Trust Co.* (Tex. Civ. App.), 198 S. W. 1047.

(c) Taxing acts must not be extended by implication.

United States v. *Wigglesworth*, 2 Story 369, Federal Case No. 16,690.
Smietanka v. *First Trust & Savings Bank*, 257 U. S. 602, 606.
United States v. *Field*, 255 U. S. 257.

(d) A taxing Act will be construed, where possible, so as to avoid double taxation.

Crocker v. *Malley*, ~~265~~ 249 U. S. ~~141~~ 223.
Cooley, Taxation, p. 165.
Tennessee v. *Whitworth*, 117 U. S. 129, 137.
Inhabitants, etc., v. *Livermore, etc. Co.*, 103 Maine 418, 69 Atl. 306, 309.

(e) A construction working great hardship, injustice, and inequality, will be avoided.

Knowlton v. *Moore*, 178 U. S. 41, 77.

(f) Doubts must be resolved in favor of the taxpayer.

Gould v. *Gould*, 245 U. S. 151.
United States v. *Wigglesworth*, 2 Story 369.
Benzinger v. *United States*, 192 U. S. 38.
American Net and Twine Co. v. *Worthington*, 141 U. S. 468.
Smietanka v. *First Trust & Savings Bank*, 257 U. S. 602, 605.

(g) A construction which raises grave constitutional questions must be avoided.

Lewellyn v. *Frick*, decided by the U. S. Supreme Court, May 11, 1925.
United States v. *Jin Fuey Moy*, 241 U. S. 394, 401.
United States v. *Delaware & Hudson*, 213 U. S. 366, 407, 408.
United States v. *Walter*, 263 U. S. 15, 17, 18.
The Abbey Dodge, 223 U. S. 166, 172.

(h) The administrative regulations under which the plaintiff has been taxed violate the proper construction of the statute.

Regulations 45, Treasury Department, Articles 1502, 1503.

Revenue Act of 1918, Title XIII, Sec. 1309 (40 Stat. p. 1143).

Morrill v. *Jones,* 106 U. S. 466, 467.

United States v. *United Verde Copper Co.,* 196 U. S. 207, 215.

II.

If a proper construction of the Revenue Act of 1918 requires the plaintiff to pay corporate income and profits taxes, the result is an unconstitutional levy and collection of taxes.

4. This is a proper action, prosecuted by proper parties, to raise the constitutional questions presented, and notwithstanding the decision of the trial court to the contrary is the only action in which such questions can be raised.

Texas, Act of 1907, Ch. 128, Secs. 1-6, Vernon's Sayles' Civil Statutes, 1914 Title 102, Ch. 2, Articles 6149 to 6154.

Mayhew & Isbell L. Co., v. *Valley Wells Truck Growers Ass'n* (Tex. Civ. App.) 216 S. W. 225, 229.

San Antonio Fire Fighters Local Union No. 84 v. *Bell,* (Tex. Civ. App.), 223 S. W. 506, 508.

5. The Act, if so construed and applied, levies a direct tax upon the Burk-Waggoner Oil Association; this tax is not levied upon income and is not apportioned

among the several states and is therefore unconstitutional.

(a) The Burk-Waggoner Oil Association is not an entity, but the property and income involved was the property and income of its members.

Pollock's Digest of the Law of Partnership, pp. 23-24.

Texas, Act of January 20, 1840, Vernon's Sayles' Civil Statutes, 1914, Title 81, Ch. 1, Art. 5492.

Wiggins v. *Blackshear*, 86 Texas 665.

Glasscock v. *Price*, 92 Texas 271, 47 S. W. 965.

Martin v. *Hemphill*, (Commission of Appeals, Texas) 237 S. W. 550, 553.

McFaddin v. *Texas Rice Land Co.*, (Tex. Civ. App.), 253 S. W. 916, 926.

Francis v. *McNeil*, 228 U. S. 695.

Bates, Law of Partnership, Vol. 1, p. 88, par. 72.

Burton v. *Grand Rapids School Furn. Co.* (Tex. Civ. App.) 31 S. W. 91, 92.

Slaughter v. *American Baptist Publication Society*, (Tex. Civ. App.) 150 S. W. 224.

Brotherhood of Railroad Trainmen v. *Cook*, (Tex. Civ. App.), 221 S. W. 1049, 1050.

Williston on Contracts, Vol. 1, p. 582, par. 307.

United Mine Workers of America v. *Coronado Coal Co.*, 259 U. S. 344, 391.

Mayhew & Isbell L. Co., v. *Valley Wells Truck Growers Ass'n*, (Tex. Civ. App.) 216 S. W. 225, 229.

In re *Tidewater Coal Exchange*, 274 Fed. 1010.

Texas, Acts of 1907, ch. 128, Secs. 4, 5; Vernon's Sayles' Civil Statutes, 1914, Title 102, Ch. 2, Arts. 6152, 6153.

Edwards v. *Old Settlers Ass'n*, (Tex. Civ. App.) 166 S. W. 423, 426.

Clark v. *Brown* (Tex. Civ. App.) 108 S. W. 421, 433.

Great Southern Fire Proof Hotel Company v. *Jones*, 177 U. S. 449.

Chapman v. *Barney*, 129 U. S. 677, 682.

Roundtree v. *Adams Express Company*, 165 Fed. 152.

Saunders v. *Adams Express Company*, 136 Fed. 494.

O'Marrow v. *State* (Tex. Crim. App.), 147 S. W. 252.

McCrary v. *State* (Tex. Crim. App.), 103 S. W. 924.

Wallace v. *People*, 63 Ill. 451, 452.

People v. *Brander*, 244 Ill. 26, 91 N. E. 59.

Hardee v. *Adams Oil Ass'n* (Tex. Civ. App.), 254 S. W. 602, 605.

Wrightington, Unincorporated Associations, p. 102, 103.

Cyc. Vol. 23, p. 472.

Brodage v. *Greenwood, et al.* (Tex. Civ. App.) 261 S. W. 453.

Claggett v. *Kilbourne*, 66 U. S. 346, 348.

Solicitor's Opinion, No. 149, Int. Rev. Cum. Bul. II-1, 1923, p. 20, 22-23, 24.

(b) Income can be taxed by Congress without apportionment only to the owner thereof; to all others it is not income within the purview of the Sixteenth Amendment to the Constitution.

Eisner v. *Macomber*, 252 U. S. 189; 213, 214, 215, 217.

Merchant's Loan & Trust Co. v. *Smietanka*, 255 U. S. 509, 515.

Stratton's Independence v. *Howbert*, 231 U. S. 399, 415.

Doyle v. *Mitchell Bros.*, 247 U. S. 179, 185.
Pollock v. *Farmers Loan and Trust Co.*, 157 U. S. 429, 158 U. S. 601.
Brushaber v. *Union Pac. R. R. Co.*, 240 U. S. 1.

(c) Congress cannot make an entity capable of owning property and receiving income out of a business group whose joint property under state laws is owned by the members individually. This would not constitute classification but would be an unlawful invasion of the state's exclusive right to regulate the ownership of property within its borders.

Constitution of United States, Tenth Amendment, Sixteenth Amendment.
King v. *American Transportation Co.*, Federal case No. 7787, 14 Fed. Cases 511, 514.
New York v. *Miln*, 11 Peters 102, 139.
Moore v. *Moore*, 47 N. Y. 467, 468-469.
Opinion of Attorney General, August 24, 1920, Treasury Decision 3071.
Solicitor's Memorandum, No. 1236, Ruling S. T. 1-20-101.
Von Baumbach v. *Sargent Land Co.*, 242 U. S. 503.
Bureau Ruling, S. T. 1-21-168.

(d) Considered as a tax imposed upon the members individually, but collected from the group, the tax must likewise fail because it is nevertheless a direct tax not imposed upon income and not apportioned among the states, and is so arbitrary and variable in its rates and application as to conflict with the Constitution.

Constitution of United States, Art. 1, Secs. 2 and 9, Fifth Amendment.
Doyle v. *Mitchell*, 247 U. S. 179.
Goodrich v. *Edwards*, 255 U. S. 527.
Knowlton v. *Moore*, 178 U. S. 41, 76-77.
Brushaber v. *Union Pacific R. R. Co.*, 240 U. S. 1, 24.

ARGUMENT.

I.

THE REVENUE ACT OF 1918, WHEN PROPERLY CONSTRUED, DOES NOT IMPOSE AN INCOME OR PROFITS TAX UPON THE BURK-WAGGONER OIL ASSOCIATION, BUT THE INCOME FROM THE ENTERPRISE WAS TAXABLE ONLY TO ITS INDIVIDUAL MEMBERS AS THE INCOME FROM A PARTNERSHIP.

1.

The Burk-Waggoner Oil Association is a partnership.

The important features of the articles of association are that those who executed the articles, as well as the others who subsequently became parties thereto by reason of accepting certificates of interest therein, joined together and contributed property or money to a common fund to engage in a joint enterprise for profit, the property and profits to belong and go to the members in proportion to their contributions. This makes of the enterprise a partnership and the members partners.

The correctness of this statement is to be determined by the laws and decisions of the State of Texas where the enterprise was created, where the joint property was located and where its business was conducted. The term "partnership" has reference to the relationship or status created by contract, the most important consequences of which are the duties and obligations of the parties to each other, their liability to third persons, and their interests in the property held under the contract. As a contract, clearly the law of the place of execution and performance must govern the mutual

rights and obligations of the parties. The law of the contract, together with the law of the place where the operations are carried on, must govern the liability of the parties to third persons. The law of the place where the property is located, as supplemented by proper terms of the contract, must determine the character of the ownership of property under the contract. In the present case, however, all of these aspects of the relationship are governed by the same law, that of the State of Texas. Regarding the term "partnership" as descriptive of the status of or relationship between the members, the liability of the members to third persons, or the character of the group interest in or ownership of property, the law of Texas leaves no doubt that from any or all possible points of view the Burk-Waggoner Oil Association was a partnership.

The most recent decision on the question is the case of *Thompson* v. *Schmitt*, 114 Texas ....., decided by the Supreme Court of Texas on June 24, 1925. This case goes much further than the decisions of some other states, for instance Massachusetts, and holds that in Texas such enterprises, regardless of the measure of control retained by the contributors of the joint fund, are partnerships; not that they are similar to partnerships, or that the members are liable like partners—but such enterprises are partnerships. Of course the question of control is not involved in the present case, for by Article XIV (R. p. 21) final control of the Burk-Waggoner Oil Association was vested in the owners of a majority of the shares.

The case above referred to went to the Supreme Court of Texas upon certified questions, the first of which was—

> "Does the declaration of trust and/or amendments thereto, of the Dixie Cooperative Mail Order House, when viewed in the light of the facts hereinbefore set forth, constitute a partnership?"

After a full discussion of the question the Court said:

> "We answer to the 'First Question' that the so-called declaration of trust, as amended, of the Dixie Cooperative Mail Order House, **created a partnership.**"

This case, therefore, cannot be regarded merely as a decision to the effect that, apart from the nature of the relationship or the existence of any statutes, certain persons were *liable as partners* or certain property should be *treated as partnership property.* It represents the most authoritative possible declaration of the law of Texas to the effect that in that state the organization of an enterprise like the Burk-Waggoner Oil Association results in the creation of a partnership status or relationship, and that the liability of the parties, the ownership of the property, and the other incidents of such relationship follow from and because of the existence of the partnership. This is even more clearly demonstrated upon further examination of the opinion, which states:

> "An unbroken line of decisions of this court declares in unmistakable terms that such persons **are members of a partnership** and cannot escape liability as partners for a debt to a third person contracted for their benefit and by their authorization.
>
> As late as 105 Texas, at pages 571, 572, in the case of *Freeman* v. *Huttig Sash and Door Co.,* the court announced that even a tacit agreement creating a community of interest in a common enterprise, to be operated for the joint account, rendered the parties to the agreement partners, when they had a right to share in anticipated profits of the enterprise. The court there further pointed out that parties could not assume relationships which amounted to partnerships in law without becoming liable as partners, though there was no agreement to become partners in name.
>
> As early as tenth Texas, the court had said that 'the criterion by which to determine, in general,

whether persons are partners or not is to ascertain whether there is a communion of profit and loss between them.' *Goode* v. *McCartney,* 10 Texas, 194, 195."

After reviewing a number of other authorities in support of its view as to the test of the relationship between the parties as such, the court further considered the significance of and effect upon the ownership of the common property of the enterprise, as follows:

"So far as the title acquired by the trustees is concerned, we think the articles as a whole disclose that they held as agents merely. If we are mistaken, then it is certainly true, as declared by the Supreme Judicial Court of Massachusetts through Chief Justice Rugg, in *Peabody* v. *Treasurer and Receiver General,* 215 Mass. 131, that 'while the legal title is in the trustee, their ownership is fiduciary, and the certificate holders are the ultimate proprietors of the property, which is held and managed for their benefit and which must be divided among them at the termination of the trust. Their rights constitute not choses in action but a substantial property right.' With certificate holders occupying the relation to the property of its **actual and ultimate proprietors**—entitled to remedies enforcing their rights as such—we cannot assent to the doctrine that they lack anything in the way of interest in or control over the property which would warrant our refusal to consider them partners."

The court further held that, in view of the established law of Texas, the attempt of the parties to limit their liability was ineffective. The court said:

"We answer to the 'Fifth Question' that Articles 6126 to 6154 of the Revised Statutes do prohibit any limitation of partnership liability to creditors in the manner shown by the facts certified.

The agreed facts which fasten on appellant the obligations of a partner to a creditor selling goods to the Mail Order House, through its authorized purchasing agents, are: First, that such agents bought appellees' goods for the House in the ordinary

course of trade and have not paid for them; second, that at the time the goods were purchased appellant was the holder of certificates of beneficial interest in the House; and third, that appellees sold the goods without expressly agreeing to look only to the assets of the Mail Order House, though with knowledge of the terms of the original declaration of trust."

The same conclusion was announced by the Supreme Court of Texas upon the same day in the case of *Victor Refining Company* v. *City National Bank of Commerce, et al.,* 114 Tex. ....., in which there was involved articles of association more closely resembling those of the Burk-Waggoner Oil Association in the degree of control vested in the shareholders.

That such an enterprise cannot hold real property in Texas has been decided by *Edwards* v. *Old Settlers Association,* (Tex. Civ. App.) 166 S. W. 423, 426, and *Clark* v. *Brown,* (Tex. Civ. App.) 108 S. W. 421, 433.

That such an organization is a partnership is not peculiar to the law of Texas, nor is this term used in the above authorities in any sense different than it is commonly used in the law and should be used in the construction of the Revenue Act of 1918. The most authoritative definition of partnership is of course that found in the decision of this court in *Meehan* v. *Valentine,* 145 U. S. 611, 618, 623, which is:

"The requisites of a partnership are that the parties must have joined together to carry on a trade or adventure for their common benefit, each contributing property or services, and having a **community of interest in the profits.** * * *

In the present state of the law upon this subject, it may perhaps be doubted whether any more precise general rule can be laid down than, as indicated at the beginning of this opinion, that those persons are partners, who contribute either property or money to carry on a joint business for their common benefit, and who **own and share the profits** thereof in certain proportions."

In *Merchants National Bank* v. *Wehrmann*, 202 U. S. 295, 300. Mr. Justice Holmes, speaking for this court, treated such an enterprise as a partnership and held that it was an *ultra vires* act for a national bank to become the owner of shares therein.

Any argument that the plaintiff was not a partnership must proceed from the assumption that the existence of partnership relationship depends upon the existence of such incidents as mutual agency, non-transferable shares, and dissolution by death or incapacity. Obviously this is fallacious, since such incidents, when they exist, are the result of the relationship and not the cause of it. The definition above quoted from *Meehan* v. *Valentine* does not refer to these incidents as a test of the existence of the relationship but relies entirely upon the contribution of capital and upon owning and sharing the profits. So long as this essential element of community of interest in profits is retained, any or all of the usual consequences may be altered or abrogated at will by the contract of the parties. As recognized by the above cited decisions of this court, there is nothing illegal in a partnership with transferable shares. In the absence of a statute so providing, there is no intermediate form of organization between a partnership and a corporation. (Bates, The Law of Partnership, Vol. I, p. 88, par. 72.) Partners may agree in advance that one of them may nominate his successor and such agreements are valid. (Id., par. 160-163.) Restrictions upon mutual agency are valid and consistent with the partnership relation. (Ruling Case Law, Vol. 20, p. 887, Partnerships, par. 98; *Winship* v. *Bank of United States*, 5 Peters 529, 8 Law Ed. 216; *Irwin* v. *Williar*, 110 U. S. 499. The same conclusion was reached by the Supreme Court of Texas, in the above cited and unreported case of *Thompson* v. *Schmitt*, in which the court said:

"It must be conceded with respect to an ordinary

> mercantile partnership, as declared by the Supreme Court of Minnesota, that the extent to which the business shall be under the management and control of any particular partner or partners is something which is expected to be arranged by the partners themselves. And, 'the **sole** management may by agreement be vested in one partner.' *McAlpine* v. *Miller,* 104 Minn., 298. This seemingly-evident truth was recognized by the Supreme Court of South Carolina when it said, 'a valid contract of partnership may be made stipulating that one of the partners would have the management of the business **to the exclusion of all the others,** and the stipulation would be good between the parties.' *Price* v. *Middleton & Ravenel,* 75 S. C., 109."

When the members of a partnership agree among themselves that shares will be transferable, that death, insolvency or incapacity will not dissolve the partnership, and that one or more of the partners shall have the exclusive management of the partnership affairs, they are none the less partners.

Under the general rules relative to partnerships, under the decisions of this Court and those of the Supreme Court of Texas, as well as the decisions of many other of the highest state courts, an enterprise like the Burk-Waggoner Oil Association is a partnership.

2.

The Revenue Act of 1918 expressly provides that the members of all partnerships are taxable upon their distributive shares of the partnership income, whether distributed or not, and excludes all partnerships from liability for income and profits taxes.

Title II of the Revenue Act of 1918 (c. 18, 40 Stat. 1057, 1059) imposes an income tax upon the incomes of individuals and corporations; while Title III (40 Stat. 1088) imposes an additional income tax, styled "War-

Profits and Excess-Profits Taxes", upon the income of corporations.

By Sections 210 and 211 of Title II (40 Stat. 1062) a normal tax and surtax is imposed "upon the net income of every individual"; and, in Section 230 of the same title (40 Stat. 1075), a tax at a flat rate is imposed upon the net income of every corporation. In Section 301 of Title III (40 Stat. 1088) an additional war and excess-profits tax is imposed "upon the net income of every corporation."

In Section 218 (a) of Title II (40 Stat. 1070) it is provided:

> "Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year."

In Section 335 (c) of Title III of the Act (40 Stat. 1095) it is provided:

> "* * * Any tax paid by a partnership or personal service corporation for any period beginning on or after January 1, 1918, shall be immediately refunded to the partnership or corporation as a tax erroneously or illegally collected."

Thus by these two sections partnerships are expressly excluded from both the income tax imposed upon individuals and corporations and the war and excess-profits tax imposed upon corporations, and the partnership income is taxed only to the members individually.

That this was the deliberate plan and purpose of Congress is sufficiently demonstrated by the fact that partnerships are expressly mentioned in connection with any provisions intended to apply to them. Many other provisions in this Act, in addition to the above sections, expressly include partnerships for various purposes. Sec-

tion 224 (40 Stat. 1074) requires returns of partnerships which merely furnish information for use in connection with the individual liability of the members and call for no tax payments by the firm. When, in the Revenue Act of 1917 (Act of October 3, 1917, c. 63, 40 Stat. 300, 303) Congress intended to levy a tax upon partnerships, the tax was imposed by Section 201 upon the income "of every corporation, partnership, or individual." With equal certainty, the intention to impose no tax liability upon partnerships, without distinction between any type of partnerships, is expressed in the Revenue Act of 1918.

3.

In view of the conflict between the specific provisions of the Revenue Act of 1918, for the taxation of partnership income to the members only, and the definition of the term "corporation", one or the other must be limited; the settled rules of statutory construction require that the limitation be so applied that no partnership income should be subjected to the taxes imposed upon corporations.

The term "corporation" is defined in Section 1 of Title I of the Revenue Act of 1918 (40 Stat. 1057), which provides:

> "The term 'corporation' includes associations, joint-stock companies, and insurance companies; * * *"

Admittedly, if there were no other sections of the law to be read with this definition and it was to be construed without considering anything else, the Burk-Waggoner Oil Association might be classified as an association or joint-stock company. A similar conclusion was reached in the case of *Hecht* v. *Malley*, 265 U. S. 144, where the definition was considered in connection with the capital

stock tax imposed by Title X of the Act. In that case the Court was dealing with a title of the law imposing an excise tax and containing no references to partnerships. Under such circumstances, the conclusion was reached that certain associations, even though partnerships, were subject to the capital stock tax. But other things must be considered in the present case. One of the questions here to be determined is, not the meaning to be given to the terms "associates and joint-stock companies" when dealing with a title containing no limitation upon the scope which can be given to these words, but rather to find the meaning which can be given to them when there is an express limitation which encroaches to a very considerable extent upon the possible meaning of the words.

The conclusion must be reached that, without the aid of construction and the rules therefor, there is a conflict between that portion of the Act which expressly deals with income from partnerships—all partnerships without restriction—and that portion defining "corporation" as including associations and joint stock companies. The words overlap in their broadest signification. Many joint-stock companies are partnerships. Under the definition of partnership, in the uniform partnership laws of many states, all partnerships are associations of two or more persons.

Not only does this conflict exist but there is a further conflict between the defining section referred to and those sections of the Act which require an individual to include as gross income his gains, profit and income derived from any source whatsoever. In a subsequent portion of this argument it will be shown that all partnership gain is the gain of the individual members, their income, derived by them, at the same time it is received by the partnership. Under the general provisions of Sec-

tion 213 of the 1918 Act (40 Stat. 1065), the gross income of an individual "includes gains, profits, and income * * * derived from any source whatever." This language is certainly broad enough to include a partner's gain from all sorts of partnerships, since the partnership relation presupposes that the profits and income are owned by the members. But, by other sections of the law, according to the executive interpretation, a portion of this income from any source whatsoever is not to be included by the individual but is to be taxed separately, as if it had been received by a corporation. Here, again, is a conflict requiring statutory construction.

One of two results must be reached: Either associations and joint-stock companies, when considered in connection with Titles II and III of the law, must be construed to exclude associations and joint stock companies which are partnerships, or Section 213 of the law defining gross income must be limited so that, instead of requiring the inclusion of gains, profit and income from any source whatsoever, it requires only the inclusion of gains, profit and income from any source whatsoever except from partnerships with transferable shares and a board of trustees, and Sections 218 and 335 must likewise be limited so as to apply only to partnerships without transferable shares and a board of trustees. One or the other result must be reached.

(a)

A specific provision in a statute controls over a general provision.

The Revenue Act of 1918 provides for a great variety of taxes. It is thought of most frequently as imposing an income and excess-profits tax, but in addition to these

two titles, the Act, which is divided into fourteen titles, imposes in other titles an estate tax, a tax on transportation, on beverages, on cigars and tobacco, on admissions and dues, excise taxes, special taxes, stamp taxes, and a tax upon the employment of child labor. Title I is styled "General Definitions" and in it are contained the definitions applicable to all of the other titles, while Title XIII, styled "General Administrative provisions", contains, as its title indicates, generally applicable administrative provisions.

From a consideration of the scope and structure of the Revenue Act of 1918 it is apparent that the defining clauses in Title I are general provisions and the clauses considered in Titles II and III are special provisions. The general definitions, admittedly, were designed to apply to all of the titles of the Act and to the various special forms of taxation therein imposed. Without great inconvenience and awkwardness of construction their scope could only be limited as to particular titles by exceptions or restrictions contained in each particular title. On the other hand, Sections 218 and 335 are applicable only to the respective titles in which they occur.

In addition, the words "associations and joint-stock companies" are broader than the word "partnership" and must be so considered regardless of their respective locations in the Act. All partnerships are associations but many associations are not partnerships. Some joint-stock companies are partnerships but there are many joint-stock companies, as for instance those organized under the statutes of some states, which are not partnerships.

The first applicable rule of statutory construction, is that a specific provision in a statute controls over a general provision. This rule has been stated by this Court

in the case of *United States* v. *Chase*, 135 U. S. 255, 260 as follows:

> "It is an old and familiar rule that, 'where there is, in the same statute, a particular enactment, and also a general one, which, in its most comprehensive sense, would include what is embraced in the former, the particular enactment must be operative, and the general enactment must be taken to affect only such cases within its general language as are not within the provisions of the particular enactment.' [Citing cases]. This rule applies wherever an Act contains general provisions and also special ones upon a subject, which, standing alone, the general provisions would include."

This is true in revenue legislation whether the special provision increases or decreases taxes, grants or withholds an exemption. Mr. Justice Peckham said for this Court in *Chew Hing Lung* v. *Wise*, 176 U. S. 156, 160:

> "This construction is in strict accordance with this rule that the designation of an article, *eo nomine* either for duty or as exempt from duty, must prevail over words of a general description which might otherwise include the article specially designated."

In another case, *American Net & Twine Company* v. *Worthington*, 141 U. S. 468, 474, it was held that where a tariff act imposed one rate of duty upon linen thread and another upon gilling twine, a kind of linen thread, the duty upon the twine was that fixed for that particular article and not upon a general class of linen thread. The Court said:

> "The article will be classified by its specific designation rather than under a general description. * * * but were the question one of doubt, we should still feel obliged to resolve that doubt in favor of the importer, since the intention of Congress to impose a higher duty should be expressed in clear and unambiguous language."

(b)

A construction will be adopted which will give every word of the statute a meaning without disregarding any other word or provision in it.

The limitation sought for does not destroy the meaning of the terms "association and joint-stock companies", even when applied to Titles II and III of the Act. There are many sorts of organizations properly classified as associations or joint-stock companies which are not partnerships. The partnership associations provided for by the laws of Pennsylvania are not partnerships. By the law of that state upon the subject (Penn. Stat. (1920) Arts., 16656-16684), it is provided that three or more persons may form a partnership association which will have a fixed capital to be paid in as subscribed for, that such an association may exist for twenty years and that the term of its existence may be renewed. Members are expressly exempted from all liability except for their unpaid stock subscriptions. The association may use a seal, must hold meetings each year, elects managers, can hold real estate and do even more than a corporation for there is no restriction upon the character of business or the number of businesses in which it can engage. This law requires that a certificate showing how the capital is paid in be filed and recorded. This is in addition to the customary corporations and limited partnerships usually provided for by state laws. The same character of partnership associations is found in New Jersey (Compiled Statutes, Sec. 30), Virginia, (Pollard's Code, 1904, Sec. 2878), Ohio, (Page's Rev. Gen. Code, Vol. II, Sec. 8059), and Michigan. Such enterprises are not partnerships. (See *Rouse* v. *Detroit, etc.,* 111 Mich. 251, 69 N. W. 511; *Staver* v. *Blake,* 111 Mich. 282, 69 N. W. 508; *Goodspeed* v. *Hally,* 199 Mich. 273, 165 N. W. 943; *First*

National Bank v. *Vanden Brooks,* 206 Mich. 177, 172 N. W. 582.)

Many associations have been before the courts which are not partnerships. One was involved in the tax case of *Chicago Title & Trust Company* v. *Smietanka,* 275 Fed. 60. Associations not partnerships have been before the Courts of Texas in the cases of *M. & M. Lloyds Insurance Exchange* v. *Southern Trading Company of Texas,* (Tex. Civ. App.) 205 S. W. 352, and *Crow et al.* v. *Cattlemen's Trust Company,* (Tex. Civ. App.) 198 S. W. 1047.

The Act under consideration is more than national in its scope. Citizens, wherever situated and in whatever form their investments may be, are subject to its operation, as are resident aliens. The law was framed so as to include at one place or another all of the income which they might receive. Language broad enough to cover, not only the wide variety of business enterprises which might be found in the various states, but those existing under foreign laws in which citizens or resident aliens might invest, had to be used. The proper and, perhaps, the only method of doing this is to start with general language broad enough to include all of the vast variety of enterprises which might be encountered, and, when it is desired to limit the scope of these broad provisions, to do so with an express exception. This plan can and should be carried into effect, and support for so doing is found in the rule that a statute is to be construed so as to give every word a meaning and not to destroy the meaning of any word used. The executive construction destroys to a considerable extent the meaning of the word partnership as used in Section 218 and 335. The above rule is supported by many authorities, including *Sarlls* v. *United States,* 152 U. S. 570; *Mercantile Bank* v. *New York,* 121 U. S. 138 and *Washington Market Co.* v. *Hoffman,* 101 U. S. 112.

(c)

Taxing acts must not be extended by implication.

A tax law is not to be extended by implication so as to apply in a manner not included in the clear import of the language used. The language used is to the effect that persons doing business as partners shall be taxed *only in* their individual capacity and that all *excess-profits taxes* collected from a partnership shall be immediately refunded it. The Government seeks to construe the law so as to keep from refunding excess-profits taxes collected from some kinds of partnerships, and to impose a tax upon a different basis and at rates upon those doing business as partners where their partnership agreement contains certain stipulations. This extends the operation of these two titles by an implied limitation upon the words "partners" and "partnership," "only" and "all".

Mr. Justice Storey said in *United States* v. *Wigglesworth*, 2 Story, 369, Federal Case No. 16,690:

> "In the first place, it is, as I conceive, a general rule in the interpretation of all statutes, levying taxes or duties upon subjects or citizens, not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operation so as to embrace matters, not specifically pointed out, although standing upon close analogy. • • • Revenue Statutes are in no just sense either remedial laws or laws founded upon any permanent public policy, and, therefore, are not to be liberally construed."

In *Smietanka* v. *First Trust & Savings Bank*, 257 U. S. 602, 606. Mr. Chief Justice Taft held that the Revenue Act of 1913 did not impose an income tax upon a trustee for an unborn or unascertained beneficiary, al-

though the Act disclosed a Congressional intention to impose a tax upon all income, saying:

> "A general intention of this kind must be carried into language which can be reasonably construed to effect it. Otherwise the intention cannot be enforced by the courts. The provisions of such acts are not to be extended by implication."

And he said, in the same case, of Treasury rulings that such fiduciaries were taxable,

> "This seems to us to graft something on the statute that is not there. It is an amendment and not a construction."

Notwithstanding the administrative construction adopted by the Treasury Department, Mr. Justice Pitney held in the case of *United States* v. *Field*, 255 U. S. 257, that the estate tax was not imposed upon the transfer of property through the exercise by will of a general power of appointment. In so doing he applied "the accepted canon that the provisions of such acts are not to be extended by implication."

(d)

A taxing act will be construed, where possible, so as to avoid double taxation.

Unless construed as here contended, the Act imposes a double tax upon income received from enterprises like the Burk-Waggoner Oil Associaiton. An income and profits tax is collected from such enterprises. When the remaining income is distributed by dividend or upon liquidation, the recipients of the distribution are likewise taxed upon what they receive. This is double taxation. It was so held in the case of *Crocker* v. *Malley*, ~~249~~ 244 U. S. ~~111~~ 223, which arose under the 1913 Revenue Act, and dealt with dividends from corporations. If the taxation of such dividends is double taxation, taxation of distribu-

tions from enterprises like the Burk-Waggoner Oil Association is even more so, for there is no separate entity intervening.

Admittedly Congress can impose double taxation. It does so in the case of corporations and dividends therefrom. But just as certainly as the power exists, it is never to be presumed; and where it is possible to adopt a construction which will avoid double taxation, that construction must be adopted. All presumptions are against double taxation.

Cooley in his work on taxation, page 165, said:

> "It is a fundamental maxim of taxation, that the same property shall not be subject to a double tax, payable by the same party, either directly or indirectly; and when it is once decided that any kind or class of property is liable to be taxed under one provision of the statutes, it has been held to follow as the legal conclusion, that the Legislature could not have intended that the same property should be subject to another tax, though there may be general words in the law which would seem to imply that it may be taxed a second time."

In *Tennessee* v. *Whitworth,* 117 U. S. 129, 137, Mr. Chief Justice Waite, although holding that, when not restrained by constitutional limitation, double taxation could be imposed, said:

> "Double taxation is, however, never to be presumed. Justice requires that the burdens of government shall as far as it is practicable be laid equally on all, and, if property is taxed once in one way, it would ordinarily be wrong to tax it again in another way, when the burden of both taxes falls on the same person. Sometimes tax laws have that effect; but if they do it is because the legislature has unmistakably so enacted. All presumptions are against such an imposition."

The Supreme Court of Maine in *Inhabitants, etc.* v. *Livermore, etc. Company,* 103 Maine 418, 69 Atl.

306, 309, said that double taxation is not to be upheld, "unless the statutes so clearly require it that no other construction is possible in reason."

If the Burk-Waggoner Oil Association had been treated as a partnership, the members would have paid a tax upon their respective shares of the profit. This profit would have been taxed only the one time and double taxation would have been avoided.

(e)

A construction working great hardship, injustice, and inequality, will be avoided.

The income and profits tax titles of the Revenue Act of 1918 are sometimes referred to as laws imposing "ability taxes"; and that is true in a certain sense. Undoubtedly Congress intended that ability to pay should measure to a very considerable extent the rate and amount of taxation. This ability to pay was to be ascertained by the net income of the taxable. This is reasonable and proper and has been upheld by this Court. But, by the construction which the Bureau of Internal Revenue places upon the law as applied to enterprises like the Burk-Waggoner Oil Association, this rational and fair system disappears. A splended example is furnished by the testimony in the present case. Over fifty thousand dollars was collected by the Government from the Burk-Waggoner Oil Association which would otherwise have gone to the witness, Greene. But his individual tax report showed that for the year 1919 he had no net income. Under a system professing to tax according to ability to pay and to measure that ability by net income, this large sum has been taken away from Mr. Greene, although he had no net income subject to taxation. This sufficiently illustrates the injustice, inequality and hardship

which results from the construction of the Bureau of Internal Revenue and it is apparent that, if the plaintiff's construction had been adopted, this result would have been avoided. He would have included in his individual return his distributive share of the profits of the Burk-Waggoner Oil Association, whether distributed or not, and would thereafter have paid a tax upon a net income which gave effect to his losses from other sources as well as his gain from this source.

The rules of statutory construction require the courts to adopt a construction which will avoid such an unjust result.

The rule is sufficiently stated in *Knowlton* v. *Moore,* 178 U. S. 41, 77, where Mr. Chief Justice White, then associate justice, said of an inheritance tax law:

> "We are, therefore, bound to give heed to the rule, that where a particular construction of a statute will occasion great inconvenience or produce inequality and injustice, that view is to be avoided if another and more reasonable interpretation is present in the statute. *Bate Refrigerating Co.* v. *Sulzberger,* 157 U. S. 1, 37; *Wilson* v. *Rousseau,* 4 How. 646, 680; *Bloomer* v. *McQuewan,* 14 How. 539, 553; *Blake* v. *National Banks,* 23 Wall. 307, 320; *United States* v. *Kirby,* 7 Wall. 482, 486."

(f)

Doubts must be resolved in favor of the taxpayer.

Doubts and ambiguities must be resolved in favor of the taxpayer. This proposition has been so often advanced in tax cases that it is almost commonplace, but it is submitted that the present case calls for the application of this rule which was announced in *Gould* v. *Gould,* 245 U. S. 151, *United States* v. *Wigglesworth,* 2 Story 369, *supra, Benziger* v. *United States,* 192 U. S.

38; *American Net and Twine Company* v. *Worthington*, 141 U. S. 468, *supra*, and the more recent case of *Smietanka* v. *First Trust & Savings Bank*, 257 U. S. 602, 605.

All cases of conflict in a statute are cases of doubt. Were there no doubt, there would be no conflict. That doubt admitted, the course to be pursued cannot be questioned—that doubt must be resolved in favor of the taxpayer.

(g)

A construction which raises grave constitutional questions must be avoided.

There still remains a rule of statutory construction before which all other rules must give way. This rule is that where one construction of a law raises grave questions as to its constitutionality, that construction must be avoided. When the application of this rule is called for, even express language not conflicting with the remainder of the Act and not otherwise requiring construction will be modified when it appears that conflict with a constitutional limitation may possibly be thereby avoided.

Since the remaining portion of this argument, after the discussion of this rule, deals with the proposition that the Act in question, if construed to impose a tax upon the plaintiff, results in unconstitutional taxation, the arguments showing how this result is brought about and that the use of this rule is called for will not be repeated here. As to this feature of the case attention is invited to the succeeding points, authorities and arguments.

That the above is correct and a paramount rule is held by many authorities. As recently as May 11, 1925,

this Court, through Mr. Justice Holmes, in the case of *Lewellyn* v. *Frick*, said,

> "We do not propose to discuss the limits of the powers of Congress in cases like the present. It is enough to point out that at least there would be a very serious question to be answered before Mrs. Frick and Miss Frick could be made to pay a tax on the transfer of his estate by Mr. Frick. There would be another if the provisions for the liability of beneficiaries were held to be separable and it was proposed to make the estate pay a transfer tax for property that Mr. Frick did not transfer. Acts of Congress are to be construed if possible in such a way as to avoid grave doubts of this kind. *Panama R. R. Co.* v. *Johnson*, 264 U. S. 375, 390."

The same Justice in *United States* v. *Jin Fuey Moy*, 241 U. S. 394, 401, said:

> "A statute must be construed, if fairly possible, so as to avoid not only the conclusion that it is unconstitutional, but also grave doubts upon that score."

It was stated as to this rule in *United States* v. *Delaware & Hudson Company*, 213 U. S. 366, 408:

> "And unless this rule be considered as meaning that our duty is to first decide that a statute is unconstitutional and then proceed to hold that such ruling was unnecessary because the statute is susceptible of a meaning, which causes it not to be repugnant to the Constitution, the rule plainly must mean that where a statute is susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter. *Harriman* v. *Interstate Commerce Commission*, 211 U. S. 407."

By reason of this ruling the phrase in a statute, "any corporation in which the United States of America is a stockholder," was limited to mean only those corporations which are instrumentalities of the Government and

in which, for that reason, it owned stock. In *United States* v. *Walter*, 263 U. S. 15, 17, 18, it was said:

> "It is said, however, that the words 'any corporation in which the United States of America is a stockholder' are too clear to be cut down. *Butts* v. *Merchants Transportation Company*, 230 U. S. 126, 136, 137. But against the cases that decline to limit the generality of words in order to save the constitutionality of an Act are many others that imply a limit, and, when the circumstances permit, the latter course will be adopted. Language as absolute as that before us was limited in *The Abbey Dodge*, 223 U. S. 166, 172."

In the case last cited, the words, "Any sponges taken * * * from the waters of the Gulf of Mexico or Straits of Florida," were construed to exclude any waters within the territorial jurisdiction of Florida. The words which were limited in these cases are much clearer in their signification and meaning than the terms "associations" and "joint-stock companies".

We will endeavor to show that merit exists in the contention that the executive construction of the Act results in unconstitutional taxation. If there is merit in this proposition, or even if there is grave doubt upon the matter, unquestionably the cases above referred to require this Court to hold that the provisions of Sections 218 and 335, expressly excluding partnerships from taxation as such, limit the definition of corporations in its application to Titles II and III of the Revenue Act of 1918, and require in the present case that the individual members of the Burk-Waggoner Oil Association pay taxes upon their distributive share of its profits—impelling the conclusion that no tax should have been collected from the Burk-Waggoner Oil Association under Titles II and III of the Revenue Act of 1918.

(h)

The administrative regulations under which the plaintiff has been taxed violate the proper construction of the statute.

The proper construction of the statute has obviously been disregarded by the administrative regulations under which the tax here involved has been collected from the plaintiff. These regulations, known as Regulations 45, purport to recognize that partnerships are not taxed, by providing that "partnerships as such are not subject to taxation under the statute", and that the term "corporation" does not include "partnerships properly so-called." This rule, however, is not consistently applied but is qualified and restricted without warrant in the statute by Articles 1502 and 1503 of Regulations 45, which provide:

> "ART. 1502. **Association.**—Associations and joint-stock companies include associations, common law trusts and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the members or shareholders on the basis of the capital stock which each holds or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization.
>
> "ART. 1503. **Association Distinguished from Partnership.** An organization the membership interests in which are transferable without the consent of all the members, however, the transfer may be otherwise restricted, and the business of which is conducted by trustees or directors and officers without the active participation of all the members as such, is an association and not a partnership. A partnership bank conducted like a corporation and

> so organized that the interests of its members may be transferred without the consent of the other members is a joint-stock company or association within the meaning of the statute. A partnership bank the interests of whose members cannot be so transferred is a partnership."

The only authority which the Bureau of Internal Revenue has for the adoption and enforcement of regulations is contained in Section 1309 of the Revenue Act (40 Stat. 1143), which is found in Title XIII thereof. This section provides:

> "That the Commissioner with the approval of the Secretary is hereby authorized to make all needful rules and regulations for the enforcement of the provisions of this Act."

The making of regulations *for the enforcement* of the Act is the ultimate limit of the authority delegated. No legislative authority was granted or could be. When anything beyond the proper scope of enforcement is attempted, the attempt is futile and illegal. The sections excluding partnerships from the income and profits taxes are to be enforced by regulations as much as any other portion of the law; and the scope of these sections cannot be limited by regulations.

The basis of the distinction made by these articles, which in substance makes transferable shares and organization with a Board of Trustees the test of partnerships, has been seen to be without foundation in the Revenue Act or in the general law of partnership. The effect of these regulations is therefore to limit the meaning of the word "partnership" as used in Sections 218 and 335 of the Act. Obviously the purpose, intent and effect of the regulations is therefore to legislate—not to enforce.

This Court has held so emphatically against executive authority to thus limit the acts of Congress that citation of authority is hardly necessary. In *Morrill* v. *Jones,*

II.

IF A PROPER CONSTRUCTION OF THE REVENUE ACT OF 1918 REQUIRES THE PLAINTIFF TO PAY CORPORATE INCOME AND PROFITS TAXES, THE RESULT IS AN UNCONSTITUTIONAL LEVY AND COLLECTION OF TAXES.

4.

This is a proper action, prosecuted by proper parties, to raise the constitutional questions presented, and notwithstanding the decision of the trial court to the contrary is the only action in which such questions can be raised.

The learned trial judge held that the plaintiff in this cause could not urge the constitutional questions raised in the pleadings because:

> "The stockholders of the plaintiff whose rights are said to be affected in this case, and for whom the plaintiff is solicitous in this suit, are not parties to the litigation and would not be bound by any determination reached herein."

We submit that this holding was erroneous, both for the reason that the stockholders in the Burk-Waggoner Oil Association are bound by the decision and for other reasons which will be first discussed.

In the first place, the constitutional points raised are based not only on the effect of the law as administered upon the shareholders separately, but also on the effect upon the group. The point is squarely made in the petition:

> "Plaintiff alleges that * * * any and all profits received from the operations conducted by plaintiff was the income of the various members of said enterprise in an amount proportionate to their interests * * *. The collection of said tax from

> plaintiff is unconstitutional * * * in that the said tax is not based upon income and is not in proportion to population;" (Rec., 2, 3).

This was intended to and does allege that because the plaintiff had no income it could not be subjected to a direct tax which was not levied on income and which was not apportioned. In addition to this, it was alleged:

> "That the individual members of the plaintiff have, by said collection, been subjected to unlawful and unconstitutional taxation because." etc. (R. p. 3)

The effect, both on the group and the several members, was alleged as a basis for holding the law unconstitutional.

The suit was to recover money paid to the defendant. Whose money? The owner of the money is undoubtedly the person who is qualified to sue for its recovery and is entitled to raise any question necessary to a proper determination of such suit. The money paid to Hopkins, Collector, was paid from partnership funds, was paid by and for the Burk-Waggoner Oil Association, belonged to the members as a group and the right of recovery, regardless of the grounds of recovery, belongs likewise to the members as a group.

It is certainly clear that the group, the partnership, the association, or whatever it may be termed, must prosecute the suit. Except under unusual circumstances a cause of action belonging to a partnership must be prosecuted in the names of all of the members. Certainly one interested in the partnership to the extent of one-tenth of the amount due to the partnership cannot bring a suit for one-tenth of the amount due to the partnership. Prior to the adoption of the law permitting suits in their distinguishing names, the same rule applied to those partnerships which were likewise associations.

This law did not attempt to subdivide causes of action among the members of an association. It gave for convenience a right to use an abbreviation—the distinguishing name—which stood for all of the members.

As well after as before the act in question was passed, no one or more members less than all could bring a suit to recover for the group the amount due the group. If any recovery in this case be had, for any reason, on any ground, constitutional or otherwise, it could only be had in the name of the Burk-Waggoner Oil Association or in the names of all of the shareholders, and the name "Burk-Waggoner Oil Association" means all the shareholders.

The testimony in this case shows that Greene had no net income when computed under the method provided for by the Bureau of Internal Revenue. Yet over fifty thousand dollars, which would otherwise have gone to him, was taken from the Burk-Waggoner Oil Association. If this makes the Act unconstitutional, it gives a right of action only because the joint funds were taken and gives the right to the group which owned the joint funds. Greene could not sue individually for the recovery of the money.

Therefore if this ground, this reason, for holding the law unconstitutional, cannot be raised, considered and determined in this cause, it cannot be raised or considered at all. If the Revenue Act of 1918 is unconstitutional in the respects urged because of the result which it has upon the members of an enterprise like this, all the injury that can ever be done, has been done. The money has been taken and, unless it is refunded to the Burk-Waggoner Oil Association, it can never be refunded to anyone.

So it is submitted, upon broad grounds, all of the ques-

tions raised must be considered and determined in this cause.

But the particular ground upon which the Court below placed its decision is not tenable. It was stated that the members of the Burk-Waggoner Oil Association would not be bound by the judgment. The law permitting suits in such distinguishing names provides under Section 3, Acts of 1907, Article 6151, Vernon's Sayles' Texas Civil Statutes, 1914 (*ante*, p. 15):

> "In suits by or against such unincorporated companies, whatever judgment shall be rendered shall be as conclusive on the individual stockholders and members thereof as if they were individually parties to such suits."

The Act in plain terms refutes the holding.

The purpose of the Act was to simplify and make easier the bringing and defending of suits in which such enterprises were involved. The Act did not purport to change the nature of the enterprise, nor, indeed, to make this method of bringing suits exclusive, but provided (Sec. 6; Article 6154, Vernon's Sayle's Texas Civil Statutes, 1914):

> "But the provisions of this Chapter shall be construed as cumulative merely of other remedies now existing under the law."

The courts of Texas have so held. In *Mayhew & Isbell L. Company* v. *Valley Wells Truck Growers' Association*, (Tex. Civ. App.) 216 S. W. 225, 229, the Court of Civil Appeals said,

> "* * * but the association did not constitute an artificial person, capable of contracting as a legal entity. The statute which permits an unincorporated association to sue or be sued in its association name merely furnishes a convenient method of conducting suits, without undertaking to change the legal status of the association or in any way affect the law in so far as it relates to contracts. The use

> of the name of the association, therefore, was merely for the purpose of describing, instead of naming, the men whose agent Rife purported to be. * * *
>
> In passing upon the questions relating to misjoinder and the form of the judgment, we take it that the inclusion in the pleadings and the judgment of the name of the association adds nothing, for to say that the association sued and recovered a judgment is equivalent, so far as the questions involved are concerned, to saying that the members of the association have sued and recovered judgment."

And in *San Antonio Fire Fighters Local Union No.* 84 v. *Bell,* (Tex. Civ. App.) 223 S. W. 506, 508, it is stated that this law is "based upon convenience and economy, in permitting all of the members of a joint-stock company or association to sue, in the name of the association."

Therefore Greene was as much a party to the suit as he would have been had he been named as a plaintiff and he is bound by the judgment rendered to the same extent.

It certainly cannot be seriously contended that the Burk-Waggoner Oil Association has not the right to have determined in this cause the proposition that the Burk-Waggoner Oil Association had no income, as income is used in the Sixteenth Amendment, and therefore could not be taxed under a law which based the tax upon net income and which did not provide for apportionment. As succeeding arguments will disclose, this is a question separate from the question of the unconstitutionality because of the effect of the law upon the individual members separately, which is the subject of the preceding argument. Even this ground of unconstitutionality, however, it is clearly proper to raise in this action, together with the constitutionality of the effect upon the group as a whole.

5.

The Act, if so construed and applied, levies a direct tax upon the Burk-Waggoner Oil Association; this tax is not levied upon income and is not apportioned among the several states and is therefore unconstitutional.

(a)

The Burk-Waggoner Oil Association is not an entity, but the property and income involved was the property and income of its members.

Since it has been demonstrated that the Burk-Waggoner Oil Association is a partnership, the above proposition might be stated that a partnership is not an entity but the partnership property and income is the property and income of the partners.

This is certainly the accepted view of the question. The common law recognized no entity in partnerships. The law in England upon the subject is sufficiently stated in Pollock's Digest of the Law of Partnership, page 23, where it is said:

> "The law of England knows nothing of the firm as a body or artificial person distinct from the members composing it, though the firm is so treated by the universal practice of merchants and by the law of Scotland. In England the firm-name may be used in legal instruments, both by the partners themselves and by other persons as a collective description of the persons who are partners in the firm at the time to which the description refers. * * * Nevertheless, the general doctrine that 'there is no such thing as a firm known to the law' remains in force."

The common law was adopted as the rule of decision in Texas by the Act of January 20, 1840. This Act is

still in force. It reads (Vernon's Sayles' Texas Civil Statutes, Title 81, Chapter 1, Article 5492):

> "The common law of England, so far as it is not inconsistent with the Constitution and laws of this state shall, together with such constitution and laws, be the rule of decision, and shall continue in force until altered or repealed by the legislature."

The Legislature has never seen fit to change this rule regarding partnerships and the common law remains in force upon this point. The decisions of the Supreme Court of Texas so hold.

In *Wiggins* v. *Blackshear,* 86 Texas 665, the Supreme Court, speaking through Chief Justice Stayton, said:

> "There are two theories on which it is sometimes claimed that creditors of a partnership have right to have its assets applied to payment of their claims in preference to creditors of the persons composing the firm. * * * The other theory is, that the partnership ought to be treated as a person, in contradistinction to the persons composing it, and therefore its property ought to be first subject to the payment of partnership debts, without reference to the will of the partners. But a partnership cannot be so considered, simply because such is not its nature.
>
> For partnership debts the members of the firm are jointly and severally liable, and the law recognizes no personality in a partnership other than that of the persons who compose it." (p. 668)

In *Glasscock* v. *Price,* 92 Texas, 271, the same Court said:

> "At common law, independently of statute, a partnership had no legal entity like a natural or artificial person. It was merely a status, 'the result of a contract' (Smith's Mercantile Law, 42), as is marriage." (p. 273)

And as late as 237 S. W. 550, 553, in *Martin* v. *Hemphill,* the Commission of Appeals, assisting the Supreme Court, said:

> "A partnership, at common law, is not a legal

entity, but only a contractual status. See *Glasscock* v. *Price,* 92 Tex. 271, etc., 47 S. W. 965."

The rule was reaffirmed in *McFaddin* v. *Texas Rice Land Company,* (Texas Civ. App.) 253 S. W. 916, 926, where it was said:

"It is well settled in Texas that a partnership is not a separate entity, apart from its members. 'The law recognizes no personality in a partnership other than that of the persons who compose it.' *Wiggins* v. *Blackshear,* 86 Tex. 668, etc."

This view of the law has been affirmed by this Court. In *Francis* v. *McNeil* 228 U. S. 695, Mr. Justice Holmes, speaking for the Court, said,

"However much the difference between firm and member under the statute [bankruptcy statute] be dwelt upon, the firm remains at common law a group of men and will be dealt with as such in the ordinary courts for use in which the discharge is granted." (p. 701)

No other conclusion could be logically reached from an examination of the accepted definitions of a partnership. Rowley, Elliott, Schumacker, Mechem, Pollock and Gilmore define a partnership as a relation. Story, Kent and Bates say that a partnership is a contract or a contract relation. Certainly these are conceptions diametrically opposed to the entity theory.

Nowhere do these cases or definitions limit the proposition so announced to any particular sort of partnership. It should follow therefore that they apply to an enterprise like Burk-Waggoner Oil Association, to "a partnership with transferable shares and that is all that a joint-stock company is." (Bates Law of Partnership, Vol. 1, page 88, par. 72.) Certainly the rule for one sort of a partnership logically should apply to the other. But we need not rely on logic alone.

In *Burton* v. *Grand Rapids School Furniture Com-*

pany, (Texas Civ. App.) 31 S. W. 91, decided before the 1907 law relating to suits by associations was adopted, it was said (p. 92):

> "An unincorporated association is no person, and has not the power to sue or to be sued. When such an association has been organized and is conducted for profit, it will be treated as a partnership, and its members will be held liable as partners."

This was reaffirmed in *Slaughter* v. *American Baptist Publication Society,* (Tex. Civ. App.) 150 S. W. 224.

In *Brotherhood of Railroad Trainmen* v. *Cook,* (Tex. Civ. App.) 221 S. W. 1049, 1050, the Court said:

> "In the absence of legislation, a voluntary association of this character is not regarded by the law as a person or entity."

"The common law recognized no entity in such associations." Williston on Contracts, Vol. 1, page 582, par. 307.

This rule is not changed by the statute (*ante,* p. 15) permitting suit in the distinguishing name. As held by this Court in *United Mine Workers of America* v. *Coronado Coal Co.,* 259 U. S. 344, 391, this is "after all in essence and principle merely a procedural matter." In the case of *Mayhew, etc.* v. *Valley Wells Truck Growers Association,* 216 S. W. 225, 229, *supra,* the Court of Civil Appeals, Texas, San Antonio District, said that:

> "The statute which permits an unincorporated association to sue or be sued in its association name merely furnished a convenient method of conducting suits, without undertaking to change the legal status of the association or in any way affect the law in so far as it relates to contracts."

The 1907 law adopted by the State of Texas merely changed court procedure. There was "no integration of the liabilities into a single corporate obligation." (*Tidewater Coal Exchange,* 274 Fed. 1010.) In the Sections

4 and 5 of that Act, Arts. 6152, 6153, Vernon's Sayle's Texas Civil Statutes, 1914, it is provided that judgments rendered in such suits "shall be binding on **the joint property of all the stockholders and members** thereof" but such judgments shall not be binding upon the individual property of the members unless such individual members were served with process, in which event the judgment "shall be *equally binding upon the individual property of the stockholders or members so served* and executions may issue against the property of the individual stockholders or members, as well as against the joint property". This constitutes a clear recognition by the Legislature of the fact that the property used by the association is not the property of a legal entity but is the joint property of the members. The common law rule prevails in Texas and remains unaltered by legislation or decision.

When it is considered that the 1907 law did no more than to provide that substantially the same rules which had been theretofore promulgated for suits by and against partnerships would apply to unincorporated joint stock companies, and that the Act makes no reference to property rights, provides specifically for the individual liability of members, and how that liability can be enforced, it would be difficult to say that the Act was intended to have any other effect than, as above stated, to furnish a convenient method of bringing suits, or that it intended to change the settled rules of property. There is nothing inconsistent in holding that a suit can be brought "as an entity" and in holding that the enterprise is not really an entity. That is the Bankruptcy rule. Proceedings in bankruptcy are instituted as if a partnership were an entity, but the partnership cannot be declared insolvent unless all members are, as

a rule absolutely in conflict with the fact of entity. *Francis* v. *McNeil*, 228 U. S. 695.

Such an enterprise cannot hold real property in Texas. In *Edwards* v. *Old Settlers Association*, (Tex. Civ. App.) 166 S. W. 423, 426, the Court said:

> "It is true, as contended by appellant, that the unincorporated association, as such could not become the owner of a leasehold estate; but the grant would not, for that reason, fail for the want of a grantee, as the title, where the grant is made to an unincorporated association, vests in its members."

In *Clark* v. *Brown*, (Tex. Civ. App.) 108 S. W. 421, 433, it was said:

> "Members of a voluntary unincorporated association can hold property in no other way than through the medium of trustees, acting as depositaries of the legal title, and this equitable interest entitles each beneficiary to the same voice in the management and control of the property as if he were a joint owner and holder of the legal title."

Various courts have promulgated doctrines which can only be sustained by sustaining the proposition that such an enterprise as the Burk-Waggoner Oil Association is not an entity, and therefore could not be the owner of income. The Courts of the United States hold that for jurisdictional purposes the citizenship of the members of such an association determines whether the right to sue in the courts of the United States exists where the suit is based upon diversity of citizenship.

Great Southern Fire Proof Hotel Company v. *Jones*, 177 U. S. 449.

Chapman v. *Barney*, 129 U. S. 677, 682.

Roundtree v. *Adams Express Company*, 165 Fed. 152.

Saunders v. *Adams Express Company*, 136 Fed. 494.

Again, under the laws of Texas, a partner cannot embezzle from the partnership. *O'Marrow* v. *State,* (Tex. Crim. App.) 147 S. W. 252, *McCrary* v. *State,* (Tex. Crim. App.) 103 S. W. 924, and this doctrine has been applied to associations.

In *Wallace* v. *People,* 63 Ill. 451, it was applied in an indictment for larceny from the American Merchants Union Express Company. The Court said (p. 452):

> "The rule seems to be well settled that property, vested in a body of persons, ought not to be laid as the property of that body unless such body is incorporated, but should be described as belonging to the individuals composing the company. Wharton's American Criminal Law, Sec. 1828, page 659; 2 Russell on Crimes, page 100."

And the Supreme Court of Illinois held to the same effect in *People* v. *Brander,* 244 Ill. 26, 91 N. E. 59, in which was involved an indictment for the embezzlement of property from the American Express Company, the Court saying:

> "A private joint-stock company is a partnership and nothing more. When not organized under any statute, it is a purely voluntary association of individuals, governed by the same rules of law as any other partnership."

It is held in Texas that a member of an enterprise like the Burk-Waggoner Oil Association cannot sue the association except under the same conditions that a partner could sue a partnership of which he was a member.

In *Hardee* v. *Adams Oil Association,* (Tex. Civ. App.) 254 S. W. 602, 605, the Court approved the rule stated in Wrightington on "Unincorporated Associations", pages 102, 103, which is as follows:

> "One member cannot sue another member on a firm transaction at law, unless there has been an accounting fixing the amount due, or the transaction

has otherwise been severed from the mutual obligations of the members."

The following was also approved in the same case, from Cyc. Vol. 23, page 472:

> "While an action at law cannot be maintained by one member of a joint-stock association against other members of the same association in respect to their mutual rights and liabilities as such members, yet he may betake himself to a co-ordinate forum and file a bill in equity for the adjustment of their rights and have an accounting if justice requires it."

And upon these authorities the Court said (p. 605):

> "It seems to be settled that she could not maintain a suit against her copartners or comembers of the association on a cause of action growing out of a partnership transaction until there had been an accounting and settlement of the partnership affairs."

This case was referred to and approved in the later case of *Brodage* v. *Greenwood, et al.*, (Tex. Civ. App.) 261 S. W. 453.

Judge Learned Hand said in *In Re Tidewater Coal Exchange*, 274 Fed. 1008, 1010:

> "To the creation of a person vested with rights and bound by obligations, there is always necessary, so far as I know, some fiat of the state, and such procedural changes as those provided by Sections 1919-1922 of the New York Code of Civil Procedure have not done more than change the method by which the joint property of the members may be reached."

That the rules governing property rights in the ordinary partnership apply to partnerships like the one at bar has been expressly held by this Court in *Claggett* v. *Kilbourne*, 66 U. S. 346, Law, in which it was said at p. 348:

> "The joint stock company, of which the judgment debtor in this case was a member constituted a partnership for the purpose of dealing in real estate; and

> the law governing the rights of creditors, representing the separate debts of a partner, must determine the rights of the plaintiff."

And the case went on to hold that the separate creditor of the member could reach the debtor's interest in the company by execution in the same way as if it were the ordinary partnership and, having purchased at execution sale, his remedy was to go into equity and call for an accounting.

Not the least convincing, perhaps, of the authorities available upon this point is the learned opinion of the legal adviser of the Commissioner of Internal Revenue. He was called upon to determine the legal effect of the dissolution of an association and the transfer of its property to trustees who were to hold the property in trust for the former members of the association pending its conversion. Five concerns were involved in this opinion. All of them were engaged in the oil business in Texas operating under articles closely resembling those of the Burk-Waggoner Oil Association. One of the properties involved actually adjoined the property of the Burk-Waggoner Oil Association. The learned Solicitor of Internal Revenue said (Solicitor's Opinion No. 149, Internal Revenue Cumulative Bulletin II-1, 1923, p. 20):

> "Common law joint-stock associations are recognized in Texas. *Clark* v. *Brown*, 108 S. W. 421, 433; *Industrial Lumber Company* v. *Texas Pine Land Association*, 72 S. W. 875. * * * Such associations are creatures of contract merely, existing by agreement of the shareholders. *People* v. *Coleman*, 133 N. Y. 279; 31 N. E. 96. * * *
>
> The conclusion stated results from the fact that a common law joint-stock association is not a legal entity apart from its members. *It is simply a partnership.* (*Spottswood* v. *Morris*, 12 Idaho 360, 85 Pac. 1094; *Ricker* v. *American Loan & Trust Company*, 140 Mass. 346; 5 N. E. 284; *Williams* v.

Boston, 208 Mass. 497; 94 N. E. 808; and *Willis v. Greiner*, (Texas Civ. Apps.), 26 S. W. 858.) **The rules applicable to the ownership of partnership property apply to such an association.** It follows that the property of the M Company was not property of a legal entity separate from its members, but partnership property acquired by the associates for partnership purposes, the legal title to which stood in the name of trustees for their convenience as an association. [Cites cases.] While each member of the association had no individual property interest in any specific property of the association, he and his associates were owners of an undivided equitable interest in such assets subject to the claims of creditors. [Cites cases.] The property interest of the former associates as beneficiaries under the trust was exactly the same after the transfer as before it, namely, a right to a proportionate share of the net income of the trust and to a proportionate share of the proceeds upon the sale of the assets. They were given no interests in any specific property. There was no change in the beneficial ownership of the supporting assets. The former associates, after the conveyance to the new trustees, as before, were owners of identical property interests in the same property. The only effect of the conveyance which marked the dissolution of the association was the transfer of the legal title to the assets from the trustees holding on behalf of the members as an association to other trustees who were to hold for the same parties as equitable co-owners, without associate or other relationship *inter sese*. The transfer was not a disposition of property resulting in taxable gain or deductible loss for income and excess profits tax purposes within the meaning of Section 202 of the Revenue Act of 1918, because in actual fact there was no change in the real ownership of the assets involved. There was merely a change in the form in which the identical parties owned the identical property." (pp. 22, 23, 24.)

Therefore, since by the common law a partnership was not an entity, since the common law is in effect in Texas, since the Burk-Waggoner Oil Association is a

partnership, since the rules relating to partnership property apply to all partnerships, those with transferable shares and boards of trustees as well as those without, since such an enterprise is "merely a partnership", since the members of such an enterprise are the real owners of the assets involved, the proposition announced, that the Burk-Waggoner Oil Association is not an entity but that its property and income are the property and income of the members, must be upheld.

(b)

Income can be taxed by Congress without apportionment only to the owner thereof; to all others it is not income within the purview of the Sixteenth Amendment to the Constitution.

Income has been frequently defined by this Court: "Income may be defined as the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through selling or conversion of capital assets." *Eisner* v. *Macomber*, 252 U. S. 189; *Merchants' Loan and Trust Co.* v. *Smietanka*, 255 U. S. 509; *Strattons Independence* v. *Howbert*, 231 U. S. 399, 415; *Doyle* v. *Mitchell Brothers*, 247 U. S. 179, 185. "When it becomes essential to distinguish between what is and what is not income," as the term is used in the Sixteenth Amendment, we must go back to this definition and not to "income," "gross income" or "net income" as defined in revenue laws, for "Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which it alone derives its power to legislate, and within whose limitations alone that power can be lawfully exercised." *Eisner* v. *Macomber*, 252 U. S. 189. Income must be "a gain, a profit * * * **received or**

drawn by the recipient [the taxpayer] **for his separate use, benefit and disposal;**—that is income derived from property. Nothing else answers the description." *Eisner* v. *Macomber,* 252 U. S. 189.

Ownership is an essential element of this definition and exposition of income. Only to an owner is gain received "for his separate use, benefit and disposal." Admittedly, every profitable commercial transaction gives rise to income which is taxable to someone. That taxable person can only be the owner. Each owner must have a property or interest of which his ownership is necessarily exclusive; as to each interest, whatever its character, ownership can exist at any given point of time only in one person. Therefore, starting with capacity to own, then adding the fact of ownership, we have income as the gain from capital, from labor, or from both combined, derived by the owner of the gain. If ownership of such gain is disregarded, the foundation of the definition and the resulting limitation upon the power of Congress is destroyed. The definition of income is altered, is expanded, and Congress by legislation alters the Constitution.

That an income tax is a direct tax and Congress is relieved by the Sixteenth Amendment from the necessity of apportioning it under Sections 2 and 9 of Article I of the Constitution only when it is imposed upon income as above defined, is, of course, settled by *Pollock* v. *Farmers Loan & Trust Company,* 157 U. S. 429, 158 U. S. 601; *Brushaber* v. *Union Pac. R. Company,* 240 U. S. 1, and *Eisner* v. *Macomber, supra.*

In *Eisner* v. *Macomber,* 252 U. S. 189, the court held that Congress could not levy a tax without apportionment upon stock dividends because the gain claimed to be represented by the stock dividend was not derived or

drawn from the corporate entity so as to be available to the taxpayer for his separate use, benefit and disposal. How much less does the power exist in Congress to transfer the ownership of income for taxation purposes and to say that income which in law belongs to one taxable will nevertheless be considered the income of another.

A similar contention was urged upon this Court in the Macomber case and was emphatically rejected. It was there said (pp. 213, 214, 215, 217):

> "We have no doubt of the power or duty of a court to look through the form of the corporation and determine the question of the stockholder's right, in order to ascertain whether he has received income taxable by Congress without apportionment. But, looking through the form, we cannot disregard the essential truth disclosed; ignore the substantial difference between corporation and stockholder; treat the entire organization as unreal; look upon stockholders as partners, when they are not such; treat them as having in equity a right to a partition of the corporation assets, when they have none; and indulge the fiction that they have received and realized a share of the profits of the company which in truth they have neither received nor realized. We must treat the corporation as a substantial entity separate from the stockholder, not only because such is the practical fact but because it is only by recognizing such separateness that any dividend—even one paid in money or property—can be regarded as income of the stockholder. Did we regard corporation and stockholders as altogether identical there would be no income except as the corporation acquired it; and while this would be taxable against the corporation as income under appropriate provisions of law, the individual stockholders could not be separately and additionally taxed with respect to their several shares even when divided, since if there were entire identity between them and the company they could not be regarded as receiving anything from it, any more than if one's money were to be removed from one pocket to another.

> Conceding that the mere issue of a stock dividend makes the recipient no richer than before, the government nevertheless contends that the new certificates measure the extent to which the gains accumulated by the corporation have made him the richer. There are two insuperable difficulties with this: In the first place, it would depend upon how long he had held the stock whether the stock dividend indicated the extent to which he had been enriched by the operations of the company; unless he had held it throughout such operations, the measure would not hold true. Secondly, and more important for present purposes, enrichment through increase in value of capital investment is not income in any proper meaning of the term. * * * Upon the second argument, the government recognizing the force of the decision in *Towne* v. *Eisner*, 245 U. S. 18, and virtually abandoning the contention that a stock dividend increases the interest of the stockholder or otherwise enriches him, insisted as an alternative that by the true construction of the Act of 1916 the tax is imposed not upon the stock dividend but rather upon the stockholder's share of the undivided profits previously accumulated by the corporation; the tax being levied as a matter of convenience at the time such profits become manifest through the stock dividend. If so construed, would the act be constitutional?
>
> That Congress has power to tax shareholders upon their property interest in the stock of corporations is beyond question; and that such interests might be valued in view of the condition of the company, including its accumulated and undivided profits, is equally clear. But that this would be taxation of property because of ownership, and hence would require apportionment under the provisions of the Constitution, is settled beyond peradventure by previous decisions of this Court."

Thus this court has emphasized that ownership, receipt and segregation are essential elements in the definition of income, which Congress cannot alter, and that income can only be taxed to the owner thereof.

The application of this doctrine to the instant case is

obvious. We have seen that the Burk-Waggoner Oil Association is a partnership, "merely a partnership"; that the rights of its members in its property are the same as the rights of the members of an ordinary partnership; that partnership or association property is really and actually the joint property of the members. We can, therefore, say that when the Burk-Waggoner Oil Association property was sold for $2,000,000 the members of that enterprise had the same rights in the $2,000,000 that they would have had, had their partnership relation been one in which shares were non-transferable and in which there was no board of trustees. Therefore, any income realized upon such sale was the income of the individual members.

But Congress and the Bureau of Internal Revenue have attempted to treat the situation differently. If the Burk-Waggoner Oil Association had not had transferable shares and a board of trustees, the Act would have required, according to the Bureau of Internal Revenue, that each member include in his individual tax return his pro rata part of the profits from the enterprise and pay a tax thereon. In other words, under such circumstances Congress recognizes that a partner owns an interest in the joint property and in the funds derived therefrom; that when a profit is made on a partnership transaction, each partner derives a gain from capital, from labor, or from both combined.

As to partnerships having transferable shares and a board of trustees, however, Congress, so we now assume, has provided that, when the property was sold, the members had no property interest in it and that the money received was not the joint property of the members; and, furthermore, that, when in that year or later years, that fund is distributed, a gain is then derived by the members. But we have seen that the interest of a

member of an ordinary partnership and of a member of the Burk-Waggoner Oil Association in partnership or association property is exactly identical; that the rules governing the property in one case apply in the other; that the Burk-Waggoner Oil Association is not an entity; that it is not capable of owning property; and that the division of partnership property among the partners merely transfers property from one pocket to another.

It follows, therefore, that in one case or the other the tax has been imposed upon something which is not income; that either a partner cannot be required to pay a tax upon his undistributed share of partnership profits or that, regardless of the character of the partnership, he can only be taxed upon his distributive share as received by the partnership, and that the division of the partnership funds neither enriches nor impoverishes him, segregates nothing for his separate use, benefit and disposal. One or the other horn of the dilemma must be seized, and we respectfully submit that the fundamental conception of income, the established law of partnership, the well recognized rules relative to association property, the decisions of the courts of Texas, of this Court, and even of the solicitor of internal revenue, require a decision that the income from an enterprise like the Burk-Waggoner Oil Association can only be taxed to the individual members, that they only own it, and to them alone can it be a gain derived.

It will thus be seen that what is sought in this case is not tax exemption; is not a holding that income from association transactions is not subject to an income tax. The determination sought is as to the taxable upon whom the tax liability will fall. In many cases, perhaps in most, the taxation of such income to the individuals will increase the revenues of the government rather than de-

crease them. In cases where the enterprise is continued and profits are being reinvested with consequent small distributions to members, the treatment of such enterprise as something separate and apart from their members and the failure to require the members to include their distributive shares, whether distributed or not, of the profits, furnishes an easy and comfortable way to prevent the imposition of the high surtaxes upon individual incomes. In effect, it permits the division of a taxpayer's income into two parts and brings both parts into the lower tax rates. Particularly is this true at the present time when corporate excess profits taxes no longer exist and corporations pay only a flat tax of 12½ per cent. An individual member of a partnership, who would be required by virtue of his interest in the partnership to include in an already large income his distributive share of the undistributed profits of the partnership, brings his partners together and agrees with them that shares in the partnership shall be transferable and they elect some trustees. Lo! This man's share of the partnership income is no longer his. Ownership is thereby transferred into an artificial entity of his own creation, and he has erected an effective bar to the impostion of surtaxes on this income. If his income subject to surtax, without the partnership income, was already $500,000, and his share of the profits of the partnership $100,000, he has by this simple transaction, under the 1924 rates, relieved himself of tax liability to the extent of $33,500, the difference between the additional tax he would have paid and that which the partnership would be required to pay. If this is possible, the statement of this court in *Merchants Loan & Trust Company* v. *Smietanka*, 255 U. S. 509, that "the provision of the will may be disregarded. It was not within the power of the testator to render the fund nontaxable" (p. 515) must be

strictly limited to the precise case, for we see how easy it is for one otherwise than by will to render a fund to a very large extent non-taxable. The power of individuals to create by private contract artificial taxable entities should be emphatically denied.

(c)

Congress cannot make an entity capable of owning property and receiving income out of a business group whose joint property under state laws is owned by the members individually. This would not constitute classification but would be an unlawful invasion of the state's exclusive right to regulate the ownership of property within its borders.

We have seen that the true conception of income is based upon ownership and that Congress is without power to extend the meaning of income as used in the 16th Amendment beyond what was understood as its meaning at the time the amendment was adopted. We have also seen that what this meaning of income is has been definitely determined by the decisions of this court and is no longer open to question.

Notwithstanding these limitations upon the powers of Congress, can Congress, under the guise of classification, tax the Burk-Waggoner Oil Association as an entity?

We do not for an instant question the power of Congress to classify all recipients of income upon any reasonable basis for the purpose of imposing income taxes at different rates, granting exemptions, or any other purpose connected with the levying and collection of such taxes. But classification is simply what its name indicates it to be. Classification for income tax purposes is a subdividing of all receiving income into different

groups, and the placing of a certain sort of enterprise in a group cannot give to the enterprise, so classified, income which in fact it does not own.

Income arises from property, and income is property, governed by the laws regulating property to the same extent that other property is regulated by them.

A somewhat fanciful example will illustrate the meaning we seek to convey. Let us assume that Congress has said that the term "corporation" includes individuals who, as agents for others, collect rents on real property and has levied a tax upon these individuals at corporate rates. Without more, it would certainly not be contended that as a result the rent collected by such agents for their principals was income to them. The rents collected do not constitute he gain which such agents derive from their labor. So, even if classified as corporations, the classification by itself is futile to enable Congress to tax them upon the rents which they collect. Something more is needed. If, in addition to so classifying agents, Congress had said that there should be included in the income reported by such agents the gross amount of rents received, then we have a question not of classification, but of the right to define income and—a power still more lacking—the power to legislate respecting the ownership of property. If the power exists to so tax the receipts of an agent under the guise of classification, then Congress has the power to say that income is something more than the gain derived from property, from labor, or from both combined. This power this Court has emphatically said Congress did not have. Or Congress has the right to say that property, which under the state law belongs to one person, belongs to another for all purposes connected with Federal taxation; in other words, has the right to regulate the ownership of property within the boundaries of the state.

Certainly Congress has no legislative authority whatsoever over the ownership of property within a state. This is peculiarly one of the powers reserved to the states and the people under the Tenth Amendment to the Constitution. This want of power is so well recognized that there are very few judicial pronouncements upon the subject. In *King* v. *American Transportation Company*, Federal Case No. 7787, 14 Federal Cases 511, 514, it was said:

> "But the courts have never gone so far in their interpretation of the constitutional power of Congress to regulate commerce, as to declare that power operative upon persons and things upon land within the boundaries of state jurisdiction, nor has the principle ever been controverted, that the rights and duties of persons in relation to property are rightfully prescribed or controlled by the laws of the state within whose territorial limits it is found."

And this court said in *New York* v. *Miln*, 11 Peters, 102, 139:

> "A State has the same undeniable and unlimited jurisdiction over all persons and things within its territorial limits, as any foreign nation, where that jurisdiction is not surrendered or restrained by the Constitution of the United States."

And in the same case the court said, that if they were to attempt to say what came within the limits of the state's jurisdiction in such matters:

> "We should say that every law came within this description which concerned the welfare of the whole people of a State, or any individual within it, whether it related to their rights, or their duties; whether it respected them as men, or as citizens of the state; whether in their public or private relations; whether it related to the rights of persons or of property of the whole people of a State, or of any individual within it; and whose operation was within the territorial limits of the State, and upon the persons and things within its jurisdicton."

An illustration of this doctrine is found in *Moore* v. *Moore,* 47 N. Y. 467, 468-469. A law of Congress had provided that failure to fix revenue stamps upon a deed rendered it void, but the court said:

> "Without denying that it is within the power of taxation, conferred upon it, for Congress to lay an excise tax upon the business operations of communities, and to collect that tax by means of stamps, to be placed upon the written instruments exchanged between contracting parties, and to enforce the observance of the law, to that end, by the imposition in it of penalties for its non-observance, we are of the opinion that it is without that power to declare that a contract or conveyance between citizens of a State, affecting the title to real estate, is void, for the reason that such observance has been omitted. Apart, then, from any consideration of the sufficiency of the stamping and canceling which took place before the referee, we think that these deeds were valid, and passed to the plaintiff, an estate in fee simple absolute, etc."

Congress may say in most emphatic terms that what the state law says is the property of one person is the property of another, but that expression is futile and powerless to change the facts. The ownership of the property remains just where it was before Congress spoke. So Congress may say that certain income does not belong to one person but belongs to another or to an artificial creation of its own, but the fact remains as true as ever that the income is owned by the same person after Congress spoke as it was before. Any other conclusion permits Congress to define income at will and to legislate regarding the ownership of property.

Thus, if in the light of the above we consider the power to tax an individual who is a member of an ordinary partnership upon his undistributed share of partnership gains, we find that the real basis of this right is not the provision in the law which requires an individual to in-

clude in his gross income his distributive share of the partnership income, whether distributed or not, but is the state law where the partnership is located, which provides that partnership property is owned by the various individuals composing the partnership, that partnership property and the gain from it actually belong to these individuals. And if Congress were to attempt to change the present method of taxing the income from ordinary partnerships, it must of necessity have the power, which it does not have, to legislate away from the individual members their rights as owners and to transfer that right into an artificial entity of its own creation. The ownership of income must be accepted by the Federal Government as it is found to exist under the laws of the state.

That this is true is further demonstrated by various practices of the Bureau of Internal Revenue in administering different tax laws.

Under the laws of Texas and many other states the gain from the labor of either spouse and all property and the increase and revenues thereof, except that acquired by gift or inheritance, is, generally speaking, the joint and equal property of the husband and wife, their community property and belongs to them equally. Prior to 1920 the Bureau of Internal Revenue attempted to tax this joint income as the income of one spouse, usually the husband, but when the matter was submitted to the Attorney General of the United States, that official held (Opinion dated August 24, 1920, Treas. Dec. 3071), in substance, that the Bureau of Internal Revenue must recognize the state laws regarding the ownership of property and that one-half of the community income only could be taxed to each spouse. The opinion states:

> "Community property, under the laws of Texas, *belongs* jointly to husband and wife; *it follows* that

> the income therefrom accrues to husband and wife in equal shares."

It was on the basis of the state law of property and ownership that the Attorney General expressly rested his conclusions as to tax liability under the federal statute. And when subsequent revenue bills were before Congress, although efforts were made to have the laws written so as to include as income to one spouse the entire community income, Congress refused to do so, evidently recognizing in this instance its lack of power to treat as income for taxation purposes that which was not income to the taxable.

The same rule has been applied in the administration of estate taxes; and in those states where one-half of the property acquired since marriage belongs to the surviving spouse, the estate tax is measured by and levied upon the other one-half.

And also with respect to stamp taxes the rules of property in the various states have been respected. Under the laws of many states an oil and gas lease is held not to convey or grant an interest in the land involved but to be a license. This rule obtains in Oklahoma. A different rule, however, obtains in Texas, and an oil and gas lease is there held to convey an interest in real estate. The stamp tax title, which was a part of the Revenue Act of 1918, provides that stamps shall be affixed to a "deed, instrument, or writing, whereby any lands, tenements or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser," etc., and practically the same provision is carried forward into the 1921 and 1924 Revenue Laws. In deference to state laws the Bureau of Internal Revenue does not require that an oil and gas lease or assignment thereof, affecting lands in Oklahoma, be stamped, but does require such instruments affecting lands in Texas to be

stamped. In considering turpentine leases in the State of Florida the Solicitor of Internal Revenue expressly recognized (Ruling S. T. 1-20-101) that the question was open only because the courts of Florida had not passed upon it and that until they had done so such leases would not be regarded as conveyances of any interest in land, in accordance with the decisions of the courts of surrounding states. The law of the state, as established by decisions of the state court and recognized by this Court in the case of *Von Baumbach* v. *Sargent Land Co.* 242 U. S. 503, has also been recognized (Bureau Ruling S. T. 1-21-168) to determine that mining leases in Minnesota are not subject to stamp tax because they do not transfer any interest in land. This administrative recognition of the principle perhaps accounts for the absence of more authoritative precedents to the effect that all federal statutes imposing taxes are construed and applied upon the premise that questions of ownership of property are determined by the laws of the several states.

Therefore, since under the laws of Texas the Burk-Waggoner Oil Association is not an entity and is not capable of owning property and since by the laws of that state its property and income is in truth and in fact the property and income of its members, the income arising from its operations can only be taxed to its members; and any attempt on the part of Congress to do otherwise under the guise of classification is futile and ineffective, constituting in reality an attempt to legislate respecting the laws of property in the State of Texas.

(d)

Considered as a tax imposed upon the members individually, but collected from the group, the tax must likewise fail because it is nevertheless a direct tax not imposed upon income and not apportioned among the states, and is so arbitrary and variable in its rates and application as to conflict with the Constitution.

It may be argued that the tax in the present case is imposed not upon the supposed entity which Congress has attempted to create, and which attempt is outside of its constitutional authority, but upon the individual members and that the tax is collected from the group for convenience. Such a position, however, does not remove the conflict between the Act and the Constitution since the result is clearly a violation of Sections 2 and 9 of Article I and of the Due Process clause of the Fifth Amendment to the Constitution.

The tax is imposed, as to individuals, upon gross income less certain deductions; the gains derived from all sources are brought together and from the sum so obtained the expenses incurred in business operations are deducted, as are taxes, losses and certain other perhaps arbitrary deductions. The remainder is the income taxed, and as to all classes of taxables Congress has specified in detail the rates to be applied, these rates being based upon ability to pay, measured by this net income. Certainly, the fact that an individual may own an interest in a profitable association does not by any means indicate that he has a net income subject to taxation, *or that he has any income whatsoever.* Testimony in this case discloses an instance of a member of the enterprise involved who suffered a net loss for the year, and who, with respect to certain of his shares, actually

realized from the enterprise less than his investment therein. It is apparent that the amount of income which the various members have, varies not only according to the amount of profit which they may make from the association enterprise, depending upon their investment therein, but also according to their earnings and losses from other sources.

Thus, A, B and C own an association in equal shares. This association is engaged in the business of producing oil and in the taxable year the operations result in a profit of $6,000. Under the 1918 law, as administered by the Bureau of Internal Revenue, there would be collected from this enterprise a tax of $940, or, under the theory under discussion, $313.33 from each. Now, A has a large income from other sources, B no income or loss whatsoever from other sources, and C who is engaged on his individual account in the oil business, a loss of $2,000 from that source.

B is married and the law says that the head of a family shall be entitled to an exemption of $2,000. If he had included his share of the profits from this enterprise in his individual report, by virtue of the exemption he would have paid no tax whatsoever. Even without the exemption he would have paid only $80 in the year 1919, 4 per cent upon $2,000. There has been taken away from him $313.33, not because the law imposes a tax in that sum upon individuals with incomes of $2,000 for it does not; not because he is not entitled to an exemption granted the head of a family, because the law expressly grants it to all people in his situation; but he is so taxed because the statute is so construed as to measure his income tax liability, not by his income, but by the joint gains of an enterprise of which he is a member. He is taxed because he owns an interest in an association and

his tax liability is measured by something other than income.

The case with C is even more obvious. He had no net income whatsoever. His losses and gains offset each other and both must be considered to arrive at the true conception of income, but he is likewise taxed because he owns an interest in the enterprise, a tax based purely upon the ownership of property, not upon income, and this tax is not apportioned.

If it be contended that income may be ascertained to exist without regard to losses, let us assume that C, like the witness in this case, purchased his interest in the association at such a price that his share of the assets of the group amounted at the end of the year to less than his investment. It has been determined by this Court, in *Doyle* v. *Mitchell Brothers Company*, 247 U. S. 179, and in *Goodrich* v. *Edwards*, 255 U. S. 527, that there can be no income without gain, represented by an excess of proceeds over cost or investment. In this case, notwithstanding the operations of the group, there is no gain to C even with respect to this particular transaction of his participation in this enterprise, and yet he must contribute $313.33 to a tax alleged to be imposed upon the income of the group. This tax is necessarily an additional impairment of his capital or property, and is obviously imposed upon him with no basis other than his ownership of property. It is thus a direct tax, and being levied without apportionment, is clearly unconstitutional.

A, however, is in a happier situation. He has a large income from other sources, say, $100,000. If he had included the $2,000, his distributive share of the profits of the association, in his individual report for the year 1919, he would have paid additional surtaxes in the sum of $960 and an additional normal tax in the sum of $160, a

total of $1,120 as against the $313.33 which he pays out of association funds. At the expense of B and C he is saved $806.67; not wholly at the expense of B and C, however, because the Government under such a theory collects $200 less in taxes than it would otherwise have collected. B, C and the Treasury contribute to lift from A's shoulders a part of the tax burden which Congress said that all others who have incomes of similar size should bear.

Therefore, when we consider the tax as imposed upon the members individually but collected from the association, we find that it is applied at rates wholly at variance with the rates fixed for individuals in the Act; that the exemptions granted individuals are destroyed in some cases; that in some cases a tax is collected even though the individual has no income and therefore is imposed purely because of ownership; that it frequently increases the tax burden upon those as to whom Congress would most readily lessen the burden and decreases the tax burden where Congress is supposed to be most reluctant so to do; and all of this without any vital distinction, any sound basis, for differentiating between such individuals and those whose income is derived from sources other than such associations.

And we do not have to presume that this will result. It has resulted in the instant case. If the tax imposed be considered as imposed upon the individuals but collected from the association, then Greene has paid over $50,000 in taxes when he had no net income, when anyone else with a similar loss would have paid no taxes whatsoever. He has paid the tax simply and only because he owned an interest in the Burk-Waggoner Oil Association.

Not only is this direct taxation, not only is it imposed in the absence of income, but it is wholly arbitrary, capricious and unjust in its operation.

This situation may be emphasized by further illustrations. Let us presume that two individuals, A and B, each own a 1/5th interest in different partnerships which are engaged in the same line of business, for instance, the oil business, the only difference between the two partnerships being that B's partnership has transferable shares and a board of trustees. A's partnership is not subjected to tax; B's partnership is treated as a corporation and required to pay income and excess-profits taxes. Now if each partnership earned $50,000 in 1919 and each had invested capital so that B's concern was entitled to the excess-profits tax limitation of twenty and forty per cent, the following shows the difference in the tax situation of the two individuals, assuming that neither had any income or losses from any other source. A would make a tax report, showing his $10,000 share of the partnership profits. His tax liability would be $590. B would have no income to report individually but his partnership would have to pay a total tax of $18,660, his 1/5th of which would amount to $3,732, about six and three-tenths times the amount which A had to pay.

The single difference in the situation of the two is that B can transfer his shares without his associate's consent and not affect the enterprise. If A transfers his share and his former associates do not agree to it the partnership is dissolved. Each has the same rights in the partnership property. Each is liable *in solido* for partnership debts. Each has the same right to share in the ultimate control of the enterprise. There is nothing to distinguish between the two situations except B's right to transfer his share of the enterprise and for this right with identical income, identical exemptions, identical liabilities, and identical ownership of the enterprise, the Government imposes upon B an additional tax burden of $3,142.

But the Government does not always place a burden as the result of this right to transfer. Sometimes it rewards. If A and B had a net income of $200,000 each from other sources, each would have paid in 1919, disregarding his income from the partnerships, $93,190 in income taxes. When A includes his share of the partnership income, his liability is raised to $99,990, an increase of $6,800 but B's additional burden consists of his share of the tax paid by his partnership, $3,732. A would pay $6,800 as against B's $3,732, a difference of $3,068.

With a large income a man is rewarded in tax saving by being a member of the partnership with transferable shares; with a small income he is heavily penalized.

Again, let us assume that one man bought a share in Burk-Waggoner Oil Association early in its history at par. The total profit for the enterprise was $1,838,053.90; his portion was 1/600th of that sum or $3,063.42. Greene bought a share for $2,950, upon which his portion of the profit was $213.42. In both cases, from each share there was taken for taxes $921. The first individual had a profit over fourteen times as great as great as Greene's but his tax burden was the same, even though Greene had no net income from other sources and the other man might have had a very large one. And Greene's tax on account of this share was over four times his actual gain on this share.

Again we repeat that this is not only direct taxation which is not upon income but it is extremely arbitrary and unjust in its operation.

The illustration used by the late Chief Justice White in *Knowlton* v. *Moore*, 178 U. S. 41, is even more applicable under such circumstances. There is was sought to measure an inheritance tax imposed upon each separate legacy or distributive share by the value of the

whole estate, that portion which the person upon whom the tax was imposed received as well as that received by others. It was said (pp. 76-77):

> "But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is only worth $1,000, may be taxed, but that the rate of tax is to be determined by attributing to A's house the value of B's house which may be worth a hundred fold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated. * * * It may be doubted by some, aside from expressed constitutional restrictions, whether the taxation by Congress of the property of one person accompanied with an arbitrary provision that the rate of tax shall be fixed with reference to the sum of the property of another, thus bringing about the profound inequality which we have noticed, would not transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems."

When the tax in the present case is considered as imposed upon the individuals of the group, rather than upon the group as an entity, it is much harder to defend than the situation referred to in the above quotation. Greene has been taxed, not because he received income, for he had no net income and in this enterprise had no gross income equal to that upon which the tax has been levied, but because he owned an interest in a profitable enterprise. As to some of his shares, over 93 per cent of the profit which measures his tax liability is profit which was not gain to him and which would not have enriched him or impoverished him had the 93 per cent been double or one-half of the amount it was, because it was the gain of the prior owner of these shares, who had realized it upon their sale. His aggregate interest in the enterprise was only slightly over 9 per cent. Therefore, almost 91 per cent of the selling price and the reported

gain, which measures the tax to which Greene as a member of the group has been required to contribute, related to property in which Greene had no interest whatsoever. Yet, owing to the application of the graduated rates, the amount of such gain directly affects the rate and the amount of the tax upon Greene's interest in the enterprise. This 91 per cent might have represented very much less or very much more property or very much less or very much greater profit, without the slightest increase or reduction in Greene's gain, and yet, under the statute as construed and applied, the rate and amount of tax upon such gain depends very definitely and substantially upon the absolute amount of the gain realized from the enterprise as a whole, as well as upon the ratio between the aggregate gain and the aggregate original investment. Such a method of tax measurement is just as arbitrary and lacking in proper basis of differentiation as if it had been based upon the color of the taxpayer's hair or a difference had been made on account of the month of his nativity.

It is true that in the Knowlton case, *supra*, the court did not hold that such a method of taxation would be unconstitutional. The conclusions reached in that case rendered a decision on that point unnecessary and, in accordance with the time-honored custom of this Court, it expressly declined to decide a point not necessarily involved. But we can safely say that the avoidance of such a result was a motive strongly impelling it to adopt the construction of the Act which it did adopt. However, in the later case of *Brushaber* v. *Union Pacific R. R. Co.*, 240 U. S. 1, 24, this Court has stated that it must be conceded that where a tax was so wanting in basis for classification that it produced a gross and patent inequality, it would follow that it was not the exercise of the

power to tax but was in fact a confiscation of property in violation of the Fifth Amendment. The court said:

> "And no change in the situation here would arise even if it be conceded, as we think it must be, that this doctrine would have no application in a case where although there was a seeming exercise of the taxing power, the act complained of was so arbitrary as to constrain to the conclusion that it was not the exertion of taxation, but a confiscation of property, that is, a taking of the same in violation of the Fifth Amendment only, or, what is equivalent thereto was so wanting in basis for classification as to produce such a gross and patent inequality as to inevitably lead to the same conclusion."

It is submitted that there can be no question of the result under the circumstances described in the above extract from the opinion in *Knowlton* v. *Moore* and no question that any tax is unconstitutional which thus ignores all reasonable grounds of classification and measure of liability, and which, as suggested by the above language from the Brushaber case, therefore amounts to a confiscation of property. No case could more clearly call for the application of this principle than this one, involving a system of taxation which would impose an enormous tax upon a person who has no net income merely because he is a member of one sort of partnership while permitting another person entirely to escape taxation who is similarly situated as to the amount of his net income and all other circumstances except that the partnership to which he belongs does not have transferable shares nor a board of trustees.

There is no "basis for classification" between the two situations nor any possible benefit which one could receive and the other could not. This not only violates the due process clause of the Fifth Amendment of the Constitution, but "transcends the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems."

Office Supreme Court, U.
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WM. R. STANSBURY
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IN THE

Supreme Court of the United States

October Term, A. D. 1925

Office Supreme Court, U.
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No. 67

BURK-WAGGONER OIL ASSOCIATION,
Plaintiff in Error,

VS.

GEORGE C. HOPKINS, Collector of Internal Revenue,
Second District of Texas,
Defendant in Error.

In Error to the District Court of the United States for the Northern District of Texas.

PETITION FOR RE-HEARING BY PLAINTIFF IN ERROR.

HARRY C. WEEKS
ARNOLD R. BAAR,
Attorneys for Plaintiff in Error.

Weeks, Morrow, Francis & Hankerson,
Staley Building,
Wichita Falls, Texas;

KixMiller & Baar,
Illinois Merchants Bank Bldg.,
Chicago, Illinois;
Of Counsel.

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TO THE HONORABLE, THE SUPREME COURT OF THE UNITED STATES:

Burk-Waggoner Oil Association, plaintiff in error in this cause, respectfully moves this Honorable Court to set aside the opinion and judgment rendered herein on November 16, 1925, and to reverse the decision of the District Court in this cause. Supporting this motion, plaintiff in error respectfully says:

THE COURT ERRED IN HOLDING THAT CONGRESS COULD DISREGARD STATE LAWS REGARDING THE OWNERSHIP OF PROPERTY AND THE RIGHTS OF TAXABLES THEREIN IN IMPOSING INCOME TAXES.

THE COURT ERRED IN HOLDING THAT THE AMOUNT TAXED IN THIS CASE WAS INCOME EARNED IN THE NAME OF THE ASSOCIATION.

This Court, in the opinion delivered in this case, after agreeing with the contention of the plaintiff in error that the Burk-Waggoner Oil Association was not an entity but was under the laws of Texas a partnership, went on to say:

> **"But the thing to which the tax was here applied is confessedly income earned in the name of the association.** * * * The power of Congress so to tax associations is not affected by the fact that, under the law of a particular state, the association cannot hold title to property, or that its shareholders are individually liable for the association's debts, or that it is not recognized as a legal entity. **Neither the conception of unincorporated associations prevailing under the local law,** nor the relation under that law of the association to its shareholders, nor their relation to each other and to outsiders **is of legal significance as bearing upon the power of Congress to determine how or at what rate the income of the joint enterprise should be taxed."**

Assuming, for the purpose of this motion, that Congress intended to tax those associations which were partnerships as corporations, it follows that Congress intended to treat such associations as entities and to tax them

as such. We understand from the opinion in this case that this Court has approved this attempt and that the effect of the opinion is to say that, although the enterprise involved is technically a partnership and for all other purposes the courts will recognize that the members have the same rights in the property as other partners have, Congress is at liberty to disregard these property rules and to tax the enterprise as an entity, and to say that the profits made jointly by the members constitute, for income tax purposes, the profits of a taxable entity. This is only another method of saying that Congress can disregard ownership and property rules in levying income taxes.

Assuming this to be the Court's attitude, let us, at the risk of tediousness, state what we understand to be the difference between an association which is not an entity and an association which is an entity. In those associations which are not entities, as, for example, the ordinary partnership, the property which constitutes the capital of the group is owned by the members of the group. They have direct ownership of undivided interests in the property so that, disregarding for the moment restrictive agreements which they may have made with each other, one member can sell and convey to a third person an undivided interest in the property and he can convey this interest free and clear of the claims of unsecured creditors of the enterprise. In such a case, the obligations incurred are the direct, primary obligations of the members and the members are not secondarily liable. The members of the group at any particular time constitute, as of that time, the "actual and ultimate proprietors of the property." (Thompson vs. Schmitt, 114 Tex____, Brief for plaintiff in error, p. 28). **Each member of the group owns an undivided interest in the prop-**

erty as a tenant in common. (Hoadley vs. County Commissioner, 105 Mass. 519). Any right which creditors of the group might assert to have the joint assets applied to the payment of their debts is a right derived only through the right which the other members have to see that this is done. This derivative right cannot be exercised except by and through the other members. **When the other members have foregone this right, bona fide, creditors are precluded.** (See in this connection Case vs. Beauregard, 99 U. S. 119; Fitzpatrick vs. Flannigan, 16 Otto 648, 106 U. S. 648; Huiscamp vs. Moline Wagon Company, 121 U. S. 310; Dakota Trust & Savings Bank vs. Hansen, 5 Fed. (2nd) 915, (8th C. C. A.) **In short, where the group is not created into a legal entity under local law, each member has identically the same property interest in the property, to the extent of his proportionate interest, as he would have if he were the sole owner of the whole.** The agreement between him and and his associates is merely a contract and does not affect the gain which he derives from the property, during ownership, any more than a contract of rental with a tenant, an option to sell or any other similar contract would.

On the other hand, if the enterprise is an entity, as, for instance, a corporation, the stockholder or member has no interest whatsoever in the property of the corporation as such. His only right in the property is to have it applied to the purposes for which the entity was created and to receive pro rata, when the dividends are declared or upon dissolution, the earnings and capital. When he sells the share, he sells this right and not an interest in the property. From the inception to the termination of the enterprise, it is looked upon as entirely separate from its stockholders, so that changes in the ownership of shares have no effect upon it whatsoever.

The liability of members for debts is always secondary.

We may say, parenthetically, that whether or not the members of either sort of enterprise are liable for its debts in any way is of itself a matter of no importance in determining how the income from the enterprise can be taxed. It is important only as an aid in determining from the nature of the liability whether or not an entity exists. An entity cannot exist where there is a direct primary liability upon the part of members for all obligations.

It is certainly clear that whether an enterprise is or is not an entity is a question governed entirely by the laws of the state where the enterprise exists. In the present case, whether or not the enterprise is an entity is important in determining whether or not the members own the property directly or have merely a right to the benefits derived from the use of the property. We take it that it will not be contended that the Legislature of the State of Texas could not, if it saw fit, pass a law abolishing the principle or theory of corporate entity and providing that thereafter corporations will be considered merely as groups of individuals, so that the holder of a share of stock in a corporation should own an aliquot portion of the corporate assets. On the other hand, we believe that the Legislature of the State of Texas could enact that associations are entities; that the rights of the owners of shares would be merely to have the assets applied to associate purposes and to receive, upon dividend or dissolution, their pro rata part of the earnings and capital. **In other words, the rights of members of either sort of enterprise are fixed by the laws of the state where the enterprise exists; a partnership can be made into an entity or a corporation made into merely a joint enterprise by the will of the legislature.**

But, when the law regarding the rights of members has been fixed by the state in which the enterprise exists, we submit that it is binding even upon Congress when Congress is dealing with a subject in which property rights are necessarily involved. If Congress must recognize the fact of corporate entity in levying income taxes, it must recognize the absence of entity in levying income taxes. The same constitutional provisions which forbid destroying or disregarding forbid creating an entity.

That Congress cannot disregard the fact of entity and the resulting property rights for income tax purposes has been definitely determined by this Court, and this is in direct conflict with the statement in the opinion in this case that the concepton of unincorporated associations prevailing under the local law is of no significance in determining how the enterprise can be taxed. In Eisner vs. McComber, 252 U. S. 189, this Court held that a stock dividend declared by a corporation did not constitute taxable income or a taxable dividend to the shareholder receiving same. This decision is founded upon the corporate entity theory and this, in turn, is founded upon state law. Congress had in express terms declared that, "A stock dividend shall be considered income, to the amount of its cash value." This Court said: (page 208)

> **"Can a stock dividend, considering its essential character, be brought within the definition?** (The definition of income). To answer this, **regard must be had to the nature of a corporation and the stockholders' relation to it."**

May we ask by what law, other than the law of the state where the corporation was chartered, the nature of the corporation can be determined or the stockholders' relation to the corporation can be ascertained? **Con-**

gress has never attempted to legislate upon such a subject and unquestionably could not. The Court went on to say that the fact that profits had been made and not divided did not give: (page 209)

> "To the stockholders as a body, much less to any one of them, either a claim against the going concern for any particular sum of money, or a right to any particular portion of the assets or any share in them unless or until the directors conclude that dividends shall be made and a part of the company's assets segregated from the common fund for that purpose."

And the opinion continued: (page 214)

> "But, looking through the form, **we cannot disregard the essential truth disclosed, ignore the substantial difference between corporation and stockholder, treat the entire organiaztion as unreal, look upon stockholders as partners, when they are not such,** treat them as having in equity a right to a partition of the corporate assets, when they have none, and indulge the fiction that they have received and realized a share of the profits of the company which in truth they have neither received nor realized. **We must treat the corporation as a substantial entity separate** from the stockholder, not only **because such is the practical fact** but because it is only by recognizing such separateness that any dividend—even one paid in money or property—can be regarded as income to the stockholder."

This Court said that Congress could not treat stockholders as partners, could not ignore the separate entity; but obviously the legislature of the state where the corporation was created could make of the shareholders partners and could destroy the corporate entity. **In oth-**

er words, this Court in the McComber case held that Congress was bound by the rules of ownership with respect to corporate property and by the fact of corporate entity in levying income taxes.

That this is true is further shown by the fact that, later in the opinion, the Court overruled the case of Collector vs. Hubbard, 12 Wallace 1. In the second argument of the case, the Government contended that, by the true construction of the Act of 1916, a tax on stock dividends was imposed, not upon the stock dividend, but rather upon the stockholder's share of the undivided profits previously accumulated by the corporation, the tax being levied as a matter of convenience at the time such profits became manifest through the stock dividend. The Court said with respect to this: (page 218)

> "That Congress has power to tax shareholders upon their property interests in the stock of corporations is beyond question, and that such interests might be valued in view of the condition of the company, including its accumulated and undivided profits, is equally clear. But that this would be taxation of property because of ownership, and hence would require apportionment under the provisions of the Constitution, is settled beyond peradventure by previous decisions of this Court."

The opinion then went on to say that the Government relied upon Collector vs. Hubbard, which dealt with the Act of June 30, 1864, providing that:

> "The gains and profits of all companies, whether incorporated or partnership, other than companies specified in that section, shall be included in estimating the annual gains, profits, or income of any person, entitled to the same, whether divided or otherwise."

Collector vs. Hubbard had upheld this system of taxation and it was overruled in the following language: (pages 218, 219)

> "Insofar as this seems to uphold the right of Congress to tax without apportionment a stockholder's interest in accumulated earnings prior to dividend declared, it must be regarded as overruled by Pollock vs. Farmers Loan & Trust Company, 185 U. S. 601, 627, 628, 637. Conceding Collector vs. Hubbard was inconsistent with the doctrine in that case, because it sustained a direct tax upon property not apportioned among the states, the Government nevertheless insists that the 16th Amendment removed this obstacle so that now the Hubbard case is authority for the power of Congress to levy a tax on the stockholder's share of the accumulated profits of the corporation even before division by the declaration of a dividend of any kind. Manifestly this argument must be rejected, since the Amendment applies to income only, and what is called the stockholder's share in the accumulated profits of the company is capital, not income. **As we have pointed out, a stockholder has no individual share in accumulated profits nor in any part of the assets of the corporation, prior to dividend declared."**

And we add to this that a stockholder had no individual share in accumulated profits, nor in any particular part of the assets of the corporation, simply and only because the laws of the state where the corporation is chartered so provided.

Can it be said that, if the state law had provided that Mrs. McComber had an individual share in the accumulated profits of the corporation and a right to demand that share, this court would have held that she could not have been taxed on this stock dividend? Cer-

tainly not! But whether she has such share depended upon state law, and her rights could have been altered by state law. The conception of corporations under the local law governed the case.

Therefore, we respectfully say that so much of the opinion as states that the conception of unincorporated associations prevailing under the local law is of no importance in determining the power of Congress to tax such associations is directly in conflict with the case of Eisner vs. McComber. The case of Eisner vs. McComber announced the correct conception of the limitations existing upon the power of Congress to define and tax income, and that so much of the opinion in this case as conflicts therewith is in error.

Passing to that portion of the Court's opinion which states that the thing to which the tax was here applied "is confessedly income earned in the name of the association," we would respectfully direct the Court's attention to certain undisputed facts disclosed by the record. The profit taxed was $1,838,053.90; of this sum $1,813,488.94 was the profit, so-called, shown in the tax return from the sale of the oil and gas lease which constituted practically the entire capital of the group. This "profit" was arrived at by the following calculation:

Selling price		$2,000,000.00
Cost of property	$ 40,000.00	
Subsequent improvements and expenses of sale (net)	146,511.06	
Total cost		186,511.06
PROFIT		$1,813,488.94

(See copy of original tax return in the printed rec-

ord between pages 40 and 41). The remaining profit reported of $24,564.96, was derived from the production of oil, but, for the purpose of this motion, will be disregarded. This $40,000.00 cost of the lease represents the amount of stock issued for same. (See Article XVI, Articles of Association, Rec. p. 21). There were six hundred shares of the capital stock outstanding and these shares were freely transferred. (Rec. p. 24). Certain of the shares cost the final owner thereof, Clois L. Greene, as high as $2,950.00 per share. (Rec. p. 51). The Articles of Association show that there were eleven people interested in the enterprise at its inception and the testimony shows that about two hundred people ultimately owned shares therein. (Rec. p. 54).

The liability which Congress imposes upon associations of this character for income and excess profits taxes is imposed upon the holders of the assets at the time the tax liability accrues, which in no case can be before the end of the taxable year and is probably the date when the association's tax return is made. If one person bought a share in the enterprise when the assets of the association were worth enough so that the stock was worth par and paid par therefor, and subsequently the association was successful so that this shareholder sold this stock to another person at an increased price, the shareholder so selling would be under no liability whatsoever to the United States for any portion of the income and excess profits tax imposed upon the association. But Congress does impose the liability upon the shareholder at the time the liability for tax accrued, and does not attempt to give this last shareholder any right to recoup any part of the tax from his predecessor in ownership. The tax here dealt with is not, and does not purport to be, a tax lev-

ied in part against the preceding owner of the shares, but is levied on the final owner.

This Court has decided that under the state law this enterprise is a partnership, technically at least, that it is not an entity; and it is certainly true that the shareholders are the "actual and ultimate proprietors of the property" and that they own the property in undivided interests, as tenants in common. **It necessarily follows from this that when a share was transferred, there was transferred, in fact and law, from the seller to the purchaser an undivided interest in this oil and gas lease which at all times constituted the bulk of the associate assets.** If the enterprise is not an entity, it can only be a group of persons. With a change in the ownership of one share, it is a different group or a different association from that which it was immediately before the transfer of such share, just as a change in the membership of any partnership makes a new partnership. So, when each share changed hands there was a new association. **When the share changed hands at more or less than par, there was a variation in the cost of the purchaser's interest in the oil lease and a consequent variation in the total cost to all of the then owners.** The multiplication of this single process at varying prices gives to the last owners varying costs to their respective interests, and a very different cost than the original $40,000.00 as the total cost for all of the owners at the date of sale, at the close of the year 1919, and at the time the tax return was made. Every person who had sold his interest in the enterprise, or his shares therein, was "out of it" and he was not subjected to any part of the tax here in controversy (although, of course, he was taxed upon his individual profit and this will be referred to hereinafter).

Therefore, we say, **"the association" taxed was the group of individuals who at the close of the year 1919 owned the money from which the amount of the tax was taken and paid.** Since this is true, can it be said that the amount taxed was income "earned in the name of the association?" In other words, was it income earned in the names of the persons who were shareholders at the close of the year 1919?

It is a settled principle that the profit derived from the sale of property cannot exceed the difference between cost and selling price. In fact, this Court has very recently in the case of United States vs. Flannery, et al 268 U. S. 98, decided April 13, 1925, re-announced the proposition that **in no case can the profit or loss from the sale of property exceed the difference between cost and selling price,** and reaffirmed similar determinations made in Goodrich vs. Edwards, 225, U. S. 527, and Walsh vs. Brewster, 225 U. S. 536; see also McCaughm, Collector, vs. Ludington, 268 U. S. 106, decided April 13, 1925. Under these decisions, if a man purchased the fee simple title to a piece of real estate for $10,000 and sold it for $20,000, under no circumstances can he be taxed upon more than $10,000, for that is the ultimate gain which he could have derived from the transaction, and there can be no income without gain. We assume that no argument is necessary to support the proposition that this Court would not uphold Congress in taxing such a person under such circumstances upon the difference between what the property cost the person who sold it to the person taxed and the selling price which the taxpayer received. To illustrate, A purchased a lot for $1000.00 and sold it to B for $10,000.00; B sold it to C for $20,000.00. Would this Court permit B to be taxed upon a profit measured by the difference between the cost to A

and the selling price to C? Can it be said that B received more than a gain of $10,000.00? Would this Court permit him to be taxed upon a so-called gain of $19,000.00? We assume that these questions must be answered in the negative.

Can it be said then that the situation would be different if B bought an undivided one half interest in the property from A and D bought the other undivided one half interest from A, and they then sold jointly to C; the aggregate prices in all cases being the same as in the preceding example? Can the profit of B and D be said to include A's profit, any more than if B had purchased the entire property from A and had had no associate therein? What is true in the one case would certainly apply in the other. Likewise, the situation would not be changed because B and D might have acquired their interest at varying times, or because one might have paid proportionately a larger price than the other.

Whether B and D be taxed separately or jointly, the gain to them separately or jointly from the sale of the property cannot exceed the difference between the sums which they paid for their respective interests and the sums which they received for their respective interests. Congress has no more right to alter or define the conception of income in this respect than it had with respect to stock dividends.

This is a question, not of the power to tax them jointly, but of the power to say that their joint "income" subject to a direct unapportioned tax, is more than their joint gain. This power is expressly denied in the McComber case.

The preceding examples illustrate exactly what happened in calculating the tax liability in this case. Some

eleven men jointly acquired title to an oil and gas lease at a cost of $40,000.00. Other people acquired for varying sums interests therein from them and these original shares were sold from time to time to various persons and for varying amounts, one or more of the shares of one of the final owners costing $2,950.00.

If there had been no changes in the ownership of shares from the beginning to the end of the enterprise, it might well be said that the amount taxed was income earned in the name of the association. But this did not happen. Original and intermediate owners sold out, took their money, and withdrew from the enterprise; people purchasing from them paid increased prices over the cost to the original owners and became members of the association; **and those that held on until the last constituted "the association" taxed in this case. The tax was actually imposed upon individuals, not upon an entity.**

To go back and to tax these last owners upon a so-called "profit" measured by the difference between the cost to the original owners and the final selling price is the exact equivalent of going back (in the example above given) and taxing B and D upon a profit measured by the difference between the cost to A and the selling price to C. **This is true because there was no entity, because the owner of a share at any particular time owned an undivided interest in and to this oil and gas lease; when he sold his share, he sold an interest in this oil and gas lease, so that the gain of the persons taxed,** even though it be conceded—which we do not concede—that they can be taxed as a group, **cannot exceed the difference between the aggregate cost of the shares to the last owners and the total selling price,** for when they sold the lease in its entirety, each sold (and must necessarily have sold since he was a joint owner) his interest therein.

It is true that some of the original owners probably held their original stock until the last, but others did not, as the record positively discloses; and the principle is the same even if only one share had changed hands at an advanced price. Since Greene purchased the share which cost the original owner only $100.00 for $2,950.00, it is just as unconstitutional and illegal to disregard $2,850.00 of his purchase price as it would be had the entire amount of the shares changed hands at $2,950.00 per share.

Let us assume that this last actually happened: The six hundred shares at $2,950.00 amount to $1,770,000.00, an increase over the cost price used in calculating the tax liability of $1,730,000.00. If one or more persons had purchased all of the stock for this $1,770,000.00, unquestionably he or they would have thereby acquired title to the entire oil and gas lease. If they had re-sold the same for $2,000,000.00, his or their actual profit would have been $1,730,000.00 less than the amount upon which the tax was based. Under the cases above cited, no more than the difference between this cost and this selling price could have been taxed.

These same rules apply, even though there was in effect a contract calling for the continued existence of the enterprise. The tax liability cannot be made to depend upon this feature of the Articles of Association. An unincorporated Association can easily be formed where one or more members have the right at all times to terminate the existence of the relationship. Would this Court say that such an association could not be taxed in the same way the Burk-Waggoner Oil Association was? If it could be, the dedication of the property to certain uses for a certain period, at all times subject to termination by the will of the majority, has no bearing on the question of tax liability.

We believe that we have hereby demonstrated not only that the method used by Congress and upheld by this Court taxes income to persons other than owners, but we submit that we have demonstrated with mathematical certainty that the income taxed was much more than actual gain; that this group of last owners was taxed merely because they owned property of a certain value under certain restrictions, and not because they had made any given amount of profit. That such a tax "would require apportionment under the provisions of the Constitution is settled beyond peradventure by previous decisions of this Court." (Eisner vs. McCumber, supra.)

The essence of the situation is that Congress has taxed the gain of the original owners, the intermediate owners, and the final owners to the final owners and has not afforded the final owners the right to recoup themselves from their predecessors in ownership.

This proposition is not to be answered by asserting that the ultimate owners purchased their interests with knowledge that the Government would assert a tax liability, and therefore they should not be heard to complain. Admittedly, one may not complain where it is merely a question of misunderstanding the liability imposed by the law; but that is not the question. The members of this group have no right to complain of any tax which Congress might have levied upon their profits, even though they may have misunderstood the nature and amount of the tax. But under the Constitution they do have the right to complain when they are subjected to an income tax upon an amount which greatly exceeds their aggregate or several incomes.

Income exists independently of the view of the tax-

able or the pronouncement of Congress. When it actually exists, Congress can tax it without apportionment. When it does not exist, and it cannot exist without, or exceed, gain, this right is gone.

In the light of the above, we respectfully call the Court's attention to that portion of the brief for plaintiff in error which deals with the question of double taxation. This was not mentioned in the Court's opinion, but we would respectfully point out that the feature of double taxation was sufficient in the case of Crocker vs. Malley, 249 U. S. 223, to have this Court declare that the enterprise there involved was not an association subject to the taxes imposed upon corporations. We believe we are correct in stating that, under the decision in Hecht vs. Malley, 265 U. S. 144, this Court would declare the enterprise involved in the Crocker case an association for excise tax purposes, when no feature of double taxation is involved.

Let us assume an association in which A bought a share for $100.00, which share was then sold to B for $500.00; the assets of the enterprise were then sold so that B's pro rata portion was $1000.00, and upon this profit from the joint sale a tax equal to $200.00 per share was levied and collected from the associate assets and the balance of $800.00 then distributed to B. The Government would collect the following income taxes upon this transaction: A would be taxed individually upon his profit of $400.00, the difference between his cost and selling price; B would then contribute his pro rata part to a tax based upon the difference between a cost of $100.00 per unit of interest in the assets and a selling price of $1000.00, although his cost was actually $500.00; in other words, he would pay a tax upon his profit plus A's profit; then upon distribution B would be taxed in-

dividually upon the difference between the $500.00 cost of his share and the $800.00 received upon liquidation. This is more than double taxation—it is treble taxation. And, with more intermediate ownerships between A and B, it is more than that.

We re-affirm the statements heretofore made that the method of taxation applied to unincorporated associations in truth and in fact taxes various individuals in the same amount, although the income of one may be much greater than the income of the other, and although some of them may have no income from the particular transaction or from the total of their transactions.

Since practically all of the profit here involved was derived from the sale of an oil and gas lease, which is real estate under the laws of Texas, unquestionably the tax here involved is a direct tax and comes within the constitutional requirement of apportionment when not levied upon income, in the constitutional sense.

It was suggested at the oral argument of this case that many of the results which are deprecated by plaintiff in error likewise apply to corporations. Admittedly, from a practical standpoint this is true. Likewise it is true that from a practical standpoint, a business man recognizes no real distinction between the placing of undistributed earnings into the capital account of a corporation and the issuance of a stock dividend thereon, and the placing of the same amount to the surplus or the undivided profit account of a partnership. He considers that his financial worth has been increased in the one case as much as in the other. But there is a difference, which this Court has distinctly recognized, between the two situations—a difference of sufficient importance to have warranted this Court in holding an express

provision of the Revenue Act of 1916 unconstitutional. (Eisner vs. McComber). This principle is the principle of corporate entity, and this principle and fact of corporate entity furnish the legal justification for Congress, if it sees fit, to impose these additional hardships upon corporations and stockholders therein. The existence of this same legal principle removes the question of determining the propriety of imposing these hardships and injustices in the case of corporations and stockholders from the judicial to the legislative field. **But that these hardships can lawfully be imposed in one case by virtue of a certain principle, affords no justification for this Court upholding their imposition in another case where the same legal principle is not involved and where the benefits, which ordinarily follow the fact of incorporation and afford some additional justification for imposing these additional hardships, are not granted.**

In conclusion, we respectfully say that the laws of the state in which the taxpayers reside and in which the property involved is located have much more than "legal significance" as bearing upon the power of Congress to determine how the persons gaining income from the property can be taxed—they are absolutely controlling. By them alone can it be determined to whom interest belongs, to whom the rent from real estate belongs, what wages are and who has received them and to whom they belong. Disregarding the laws of property in the state would permit an agent to be taxed upon money received for his principal, or a bank to be subjected to an income tax based upon the amount of its deposits, and many other results equally inconsistent with the settled principles announced by this Court. And we further submit that no single individual, nor any group of individuals when

the group does not constitute an entity, can be subjected to an unapportioned income tax upon a so-called profit derived from the sale of property, the amount of which exceeds the difference between the aggregate cost and the aggregate selling price of the property.

If these statements are correct, then we submit the position taken in the original brief is unassailable; and this case should be reversed.

Respectfully submitted,

HARRY C. WEEKS
ARNOLD R. BARR,
Attorneys for Burk-Waggoner
Oil Association,
Plaintiff in Error.

INDEX

AUTHORITIES

In the Supreme Court of the United States

OCTOBER TERM, 1925

No. 67

BURK-WAGGONER OIL ASSOCIATION, PLAINTIFF IN ERROR

v.

GEORGE C. HOPKINS, COLLECTOR OF INTERNAL REVENUE, Second District of Texas

IN ERROR TO THE DISTRICT COURT OF THE UNITED STATES FOR THE NORTHERN DISTRICT OF TEXAS

BRIEF FOR THE DEFENDANT IN ERROR

The report of this case in the court below is found in 296 Fed. 492, and the opinion is printed in the Record, pages 4 to 12.

JURISDICTION

The plaintiff in error sued the Collector of Internal Revenue in the District Court to recover $145,827.67 paid as income and excess-profits taxes and interest thereon for the year 1919 under the Revenue Act of 1918 (Act of February 24, 1919, c. 18, 40 Stat. 1057), alleging that the taxes were unlawfully assessed and were paid under protest

and that claim for refund had failed. The amended petition was filed February 21, 1924. (R. 1.) The case was tried by the court without a jury, pursuant to written waiver, and resulted in a judgment, filed March 3, 1924, in favor of the defendant. (R. 12.) The case was tried upon an agreed statement of facts (R. 14), and in addition the testimony of one witness was taken (R. 49). The opinion of the court sets forth briefly (R. 5–7) the essential facts, and the entire stipulation of facts was incorporated in a bill of exceptions (R. 14 et seq.). A writ of error was allowed and filed on April 21, 1924. (R. 58, 59.)

The jurisdiction of this Court by direct writ of error to the District Court seems to be based upon Section 238 of the Judicial Code, upon the ground that the case involves the construction of the Constitution and the constitutionality of the Revenue Act of 1918.

The Government does not admit this jurisdiction and suggests that no substantial constitutional question is involved and that this Court may well dismiss the writ of error upon the authority of *Sugarman* v. *United States,* 249 U. S. 182; *Piedmont Power & Light Co.* v. *Graham,* 253 U. S. 193; *Wise* v. *Mills,* 220 U. S. 549; *American Sugar Refining Co.* v. *United States,* 211 U. S. 155, and similar cases.

STATEMENT OF THE CASE

The Burk-Waggoner Oil Association was organized on November 15, 1918, by an agreement be-

tween six individuals residing in Texas, which was styled "Articles of Association" and filed in the deed records of Wichita County, Texas. (R. 14.)

Under Article I the organizers "do hereby form an unincorporated joint stock association to be known and styled Burk-Waggoner Oil Association (hereinafter referred to as the company)," which was to continue during the lives of the subscribers and for twenty-one years after the death of the one who died last. Under Article II the general purpose of the "company" was to engage in all branches of the oil business, including the acquisition and disposition of lands. (R. 15.)

The capital stock was $60,000 divided in shares of $100 each to be evidenced by certificates. (Art. III, R. 15.) The certificates were to be issued and signed by the Board of Trustees and countersigned by the secretary of the Board (Art. IV, R. 15), and were to be in the form therein set forth, which contained the provision that no member of said "company" or owner or holder of the certificate should have any authority to transact any busness on behalf of or binding on the "company," and no member of the company should be personally liable upon any contract of any kind or upon any tort of the "company" (R. 16).

The conditions in the certificate were to be binding on each shareholder, his heirs, assigns, and legal representatives. The certificates were to be transferable only on the books of the company and only the shareholders whose certificates stood

in their name would be considered within the terms of the instrument. Any shareholder might transfer his share, and in case of loss or accidental destruction, the trustees might cause a new certificate to be issued. (Art. III, R. 16.)

The shareholders should have no right to any portion of the property or to call for any partition of the property or dissolution of the trust, and the shares should be personal property carrying the right to a proportionate division of the profits, and, upon termination or dissolution, to a proportionate division of the principal. (Art. IV, R. 17.)

The death, insolvency, or bankruptcy of a member, or the transfer of his interest should not work a dissolution or have any effect upon the business nor entitle representatives, heirs, or assigns to an accounting, but the company should remain intact and undisturbed thereby. (Art. VI, R. 17.)

The affairs of the "company" were to be managed by a board of six trustees; the signers of the certificate were to be the first trustees and were to continue until their successors should be elected by a majority of the shares, present or represented at a meeting of the shareholders, which meeting was to be held annually on the first Tuesday in December. The board was to select its president, vice president, secretary, and treasurer and might create such other officers as they might deem necessary to carry on the business of the "company." (Art. VII, R. 17.)

Title to all property acquired should be in the name of the trustees who should hold the same as joint tenants and not as tenants in common, and the trustees might sue and be sued or the "company" might sue or be sued in the company name as provided by the statutes of Texas. (Art. VII, R. 18.)

The trustees were to have full power to conduct the business and affairs of the "company," to borrow money on the credit of the "company," to issue debentures secured by mortgage on the property of the "company." Trustees might fix their own time and place of meeting and the majority should constitute a quorum. Any vacancy should be filled by the remaining members of the board, subject to the right of the shareholders to do so instead, and the board of trustees might from time to time declare and pay such dividends from the earnings of the "company" as they might deem expedient. (Art. VII, R. 18.)

The funds and property of the "company" were to stand primarily charged with the payment of all obligations of the "company" to the end that the members might be protected from personal liability. (Art. VIII, R. 19.)

The board of trustees might adopt by-laws (Art. IX, R. 19) and at any annual or special meeting called for that purpose the shareholders might amend the articles of the association by a three-fourths vote and at any such meeting by-laws

might be adopted, repealed, or amended (Art. X, R. 19). A majority of the shares then issued and outstanding should be necessary to constitute a quorum or to transact business at any such meeting. Provisions were made in Articles XII and XIII (R. 20) for the calling of special meetings of the shareholders voluntarily by the board, or when requested by the holders of one-fourth of the shares outstanding.

The members of the board were at all times subject to the orders of the shareholders, who might, by vote of a majority of the shares then issued and outstanding, remove any or all of them and appoint their successors. (Art. XIV, R. 21.)

$40,000 of the capital stock of the "company" was to be paid for the acquisition of a certain described oil and gas lease, and the balance, $20,000, was to be sold for cash (Art. XVI, R. 21), and the stock of the association might be increased at any time by vote of a majority of all the stock present and represented at a meeting called for that purpose (Art. XVI, R. 22).

The dissolution of the "company" might be effected by vote of the shareholders holding three-fourths of all the shares then issued and outstanding, but not at any time prior to the period fixed for final dissolution, while there should be outstanding against the property any obligations of the trustees secured by mortgage on the property, without the written consent of the holders of two-thirds of the bonds. (Art. XVII, R. 22.)

About two hundred persons were interested, and were certificate holders, in the association and the certificates were traded in generally by the public. (R. 7.)

The lease referred to was assigned to the trustees on December 14, 1918 (R. 25). With funds raised from the sale of the remaining capital stock, an oil well was drilled, which was very productive, and on May 5, 1919, the whole property was sold for $2,000,000. A profit of $24,564.96 was received from the production of oil prior to the sale, and a profit of $1,813,488.94 from the sale of the property, the total profit being $1,838,053.90, all of which was received in the year 1919. (R. 27.)

The total income and excess profits tax assessed was $561,279.20. This was paid in four instalments, the first three being paid to the predecessors of the defendant, against whom suits are pending, and the last instalment, $145,827.66, was paid to the defendant, and it was to recover that payment that this suit was brought. (R. 4.)

The tax was assessed upon the theory that the plaintiff was an association or joint-stock company and taxable as a corporation within the meaning of Section 1 of the Revenue Act of 1918 (Act of February 24, 1919, c. 18, 40 Stat. 1057), which provides that the term "corporation," when used in the act, should include "associations, joint-stock companies, and insurance companies."

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The plaintiff now claims that it is a partnership and not taxable as an association.

FURTHER SIGNIFICANT FACTS

In view of the claim now made that plaintiff in error is not to be treated as an association but rather as a partnership, certain other facts shown by the record are significant.

In the first place, the record affords no reason to infer that prior to the institution of this suit the members of this association ever regarded it as anything but an association taxable as such with corporations. The claim now made was not advanced in any of the proceedings to obtain a refund or revision of the tax by the Commissioner of Internal Revenue. The first claim for refund (Ex. A, R. 28) is based upon the contention that the principal item of its income was derived from the sale of capital assets and that such gain was not income within the Sixteenth Amendment. In that claim it is stated (R. 29) "claimant, Burk-Waggoner Oil Association, is an unincorporated joint-stock association, organized with a capital stock of $60,000 on November 15, 1918," and the property which it sold is described as "the company's property."

In the next claim (Ex. B, R. 29, 30) it is referred to as "said company." The claim therein made was that it was entitled to a special assessment under Sections 327 and 328 of the Act of 1918, because "owing to abnormal conditions af-

fecting the capital income of the Burk-Waggoner Oil Association it would suffer exceptional hardship, as is evidenced by the gross disproportion between the tax paid and the tax paid by representative corporations engaged in the same line of business." (R. 30.) It goes on:

> This company contends that it should be compared to representative corporations engaged in the business of producing oil; that it should not be compared only with those which are highly successful. That the term "representative corporation" means substantially average corporations, and that the average of a large number of corporations engaged in the oil business, including the very successful, the unsuccessful, and those between, should be used as a basis of comparison.

It was also contended that the average "small oil company" for the year 1919 made no money, and that the greater number of those operating in that year were then insolvent; that this applies particularly to the locality in which the Burk-Waggoner Oil Association operated, and that the "average corporation" engaged in the business in that vicinity in 1919 paid no excess profits tax.

In the original return (Ex. C) it claimed the benefit of a "discovery" under sections 234(9) and 337 of the excess profits tax law.

In a letter dated March 5, 1920, addressed to the Commissioner of Internal Revenue by attorneys for the plaintiff in error (R. 38) it is again

described as a "joint stock association" and again makes application for a special assessment of its excess profits tax under the provisions of Section 327 of the Act. This letter calls attention to the gross disproportion between the tax computed without the benefit of that section and the tax if computed by reference to "representative concerns." It bases an argument upon reports of the "larger companies," like the Standard Oil Company and the Texas Company, and submits a list of "smaller companies" whose capital "is of approximately the same size as the Burk-Waggoner Oil Association." (R. 40.) Then follows this significant sentence:

> A large number of successful concerns operating in the field operate as partnerships and for that reason their returns can not be compared with the Burk-Waggoner Oil Association. (R. 40.)

The conclusion which the Commissioner was asked to draw was that the excess-profits tax of the Burk-Waggoner Oil Association as computed without the benefit of Section 327 was grossly disproportionate to that of "representative concerns engaged in the same business." All this shows that there was never in the minds of plaintiff's officers or counsel, during the time when refund was being sought from the Treasury, any idea that plaintiff was not taxable as a corporation.

A TEXAS STATUTE

On page 15 of the brief of plaintiff in error there is set forth a statute of the State of Texas, passed in 1907, entitled: "An Act to authorize unincorporated joint stock companies or associations to sue and be sued in their company or distinguishing name and to prescribe the mode and effect of service on such unincorporated companies, and the legal effect of judgments that shall be rendered in such actions, and declaring an emergency."

The provisions of the statute are indicated by its title, and, as the court below aptly said (R. 9): "They come here under section 6149 of the Revised Statutes of Texas, which authorized an association or joint stock company to sue and be sued."

CONTENTIONS OF THE DEFENDANT IN ERROR

Defendant in error contends:

1. That the plaintiff-in-error is, within the meaning of the Revenue Act of 1918, an association or joint-stock company, and therefore taxable as a corporation, and

2. That the case presents no substantial constitutional question to sustain the jurisdiction of this Court by direct writ of error.

ARGUMENT

I

The plaintiff in error is, within the meaning of the Revenue Act of 1918, an association or joint-stock company, and therefore taxable as a corporation

Section 1 of the Revenue Act of 1918 (Act of February 24, 1919, c. 18, 40 Stat. 1057) provides that when used in the act "the term 'corporation' includes associations, joint-stock companies, and insurance companies," and subsequent sections impose upon "corporations" as thus defined income and excess-profits taxes.

The facts already stated show conclusively that the plaintiff in error is an association or joint-stock company within the meaning of the act. The decision of this Court in *Hecht* v. *Malley*, 265 U. S. 144, is ample authority. That case involved the excise-tax provisions of the Revenue Acts of 1916 and 1918, and this Court held that the organizations then before the Court were associations within the meaning of the latter act. Mr. Justice Sanford, speaking for the Court, said, at page 157:

> The word "association" appears to be used in the Act in its ordinary meaning. It has been defined as a term "used throughout the United States to signify a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of

> some common enterprise." 1 Abb. Law Dict. 101 (1879); 1 Bouv. Law Dict. (Rawle's 3rd Rev.) 269; 3 Am. & Eng. Enc. Law (2d ed.) 162; and *Allen* v. *Stevens* (App. Div.) 54 N. Y. S. 8, 23, in which this definition was cited with approval as being in accord with the common understanding. Other definitions are: "In the United States, as distinguished from a corporation, a body of persons organized for the prosecution of some purpose, without a charter, but having the general form and mode of procedure of a corporation." Webst. New Internat. Dict. (U. S.). "An organized but unchartered body analogous to but distinguished from a corporation." Pract. Stand. Dict., and see *Malley* v. *Bowditch* (C. C. A.), 259 Fed. 809, 812; *Chicago Title Co.* v. *Smietanka* (D. C.), 275 Fed. 60; also *United Mine Workers* v. *Coronado Co.*, 259 U. S. 344, 392, in which unincorporated labor unions were held to be "associations" within the meaning of the Anti-Trust Law.

That the Burk-Waggoner Oil Association is regarded for certain purposes by the courts of Texas as a partnership is immaterial. The organizations considered in *Hecht* v. *Malley* were so-called "Massachusetts trusts." This Court said (p. 147):

> Under the Massachusetts decisions these trust instruments are held to create either pure trusts or partnerships, according to

> the way in which the trustees are to conduct the affairs committed to their charge. If they are the principals and are free from the control of the certificate holders in the management of the property, a trust is created; but if the certificate holders are associated together in the control of the property as principals and the trustees are merely their managing agents, a partnership relation between the certificate holders is created. *Williams* v. *Milton,* 215 Mass. 1, 6; *Frost* v. *Thompson,* 219 Mass. 360, 365; *Dana* v. *Treasurer,* 227 Mass. 562, 565; *Priestley* v. *Treasurer,* 230 Mass. 452, 455.

This court then pointed out the provisions of the trust agreement involved in the case, and it is sufficient to say that, so far as present discussion is concerned, the Burk-Waggoner Oil Association possesses all the elements which made the Hecht, Haymarket, and Crocker Trusts "associations" within the meaning of the Act. It corresponds in every way to the definitions of association referred to by Mr. Justice Sanford in the quotation, *supra.* The fact that *Hecht* v. *Malley* arose under the excise-tax provisions makes no difference. The word "corporation" as defined in the act applies to the entire act, and there is no ground whatever for believing that it meant one thing in one portion of the act and something different in another portion.

But it is contended that because the Texas courts treat such associations as this as partnerships, it is exempted from the effect of Section 1 of the Act by Section 218 (40 Stat. 1070):

> That individuals carrying on business in partnerships shall be liable for income tax only in their individual capacity. There shall be included in computing the net income of each partner his distributive share, whether distributed or not, of the net income of the partnership for the taxable year. * * *

This presents no difficulty, however. As the word "association" appears to be used in the act in its ordinary meaning (*Hecht* v. *Malley, supra*), so also do the words "individuals carrying on business in partnership." The ordinary meaning of the words "individuals carrying on business in partnership" refers clearly to partnerships in the ordinary sense of the word and not to such organizations as the Burk-Waggoner Oil Association. Aside from the individual liability of the stockholders, which, in spite of their efforts to avoid it, the courts of Texas would probably impose, this association is lacking in the essential elements of the ordinary partnership, such as dissolution upon the death of a member, lack of power of members to bind the other members, or to dispose of their interests and foist upon the partnership new members. On the other hand, with the exception of a charter granted by the State, it possesses almost

every element of a corporation. It has a fixed capital stock divided into shares represented by certificates, transferable only upon the books of the corporation, and traded in generally by the public; its affairs are managed by a board of directors with the ordinary corporate officers. It had by-laws which could be adopted by the directors or by the stockholders. There were provisions for regular and special meetings of the stockholders, the directors were removable by the stockholders, and the ultimate power was in the stockholders. Without enumerating with more detail, it was "a body of persons organized for the prosecution of some purpose, without a charter, but having the general form and mode of procedure of a corporation," and it had by the statutes of Texas the right to sue and be sued in its association name. It was such an association as was described by Chief Jutice Knowlton in *Hussey* v. *Arnold,* 185 Mass. 202, as follows:

> The agreement creating the trust has peculiar provisions. The object of it, apparently was to obtain for the associates most of the advantages belonging to corporations, without the authority of any legislative act, and with freedom from the restrictions and regulations imposed by law upon corporations.

It was an association of the kind considered by the Supreme Judicial Court in *Opinions of Justices,* 196 Mass. 603, when that court advised the legislature that it had power to enact a law im-

posing a tax on the sale of their certificates. Justice Rugg in his opinion said:

> The device of voluntary unincorporated associations, with complicated contractual provisions for the transfer of fractional interests therein by certificates, depending for their validity upon an elaborate and intricate trust agreement, for the enforcement and interpretation of which resort is frequently and necessarily had to the courts, does not belong to that class of natural rights which is above the power of the legislature.

It was upon associations of this kind clearly that the Revenue Act of 1918 imposed the excess profits and excise taxes.

Nor does the provision of Section 335 of the act (40 Stat. 1095) cast any doubt upon this contention. Paragraph (c) of that section, a part only of which is quoted in the brief of plaintiff in error, is as follows:

> (c) If a partnership or a personal service corporation makes return for a fiscal year beginning in 1917 and ending in 1918, it shall pay the same proportion of a tax for the entire period computed under Title II of the Revenue Act of 1917, which the portion of such period falling within the calendar year 1917 is of the entire period.
>
> Any tax paid by a partnership or personal service corporation for any period beginning on or after January 1, 1918, shall be immediately refunded to the part-

nership or corporation as a tax erroneously or illegally collected.

This section appears under "Part VII—Miscellaneous" of the act. It is to be remembered that the taxes imposed by the act were to cover the *calendar year* 1918, although the act was not passed until 1919. This section made provision for an apportionment of the taxes of corporations, partnerships, and personal service corporations making returns for a *fiscal year* beginning in 1917 and ending in 1918.

Both the Act of March 3, 1917 (c. 159, 39 Stat. 1000), and the Revenue Act of October 3, 1917 (c. 63, 40 Stat. 300), imposed excess-profits taxes on corporations and partnerships, and the latter Act defined the term "corporation" as including joint-stock companies and associations. (See *LaBelle Iron Works* v. *United States,* 256 U. S. 377, 384, 387.) The Act of 1918, however, while continuing the excess-profits tax upon corporations other than personal-service corporations, including associations and joint-stock companies, did not impose it upon partnerships. A line was drawn between ordinary corporations, including associations and joint-stock companies on the one hand, personal-service corporations and ordinary partnerships on the other, and inasmuch as its provisions were retroactive to cover the calendar year 1918 it was proper to provide for an apportionment of the taxes of such taxpayers as had

paid upon a fiscal year beginning in 1917 and ending in 1918. This was the purpose of Section 335.

There is no inconsistency or ambiguity in these provisions of this Act.

II

The case presents no substantial constitutional question to sustain the jurisdiction of this court by direct writ of error

It is obvious that there is only one real question in the case: Is the Burk-Waggoner Oil Association to be classed as an association or joint-stock company or as a partnership? That is, of course, not a constitutional question. The petition alleged (R. 3) that the collection of the tax was unconstitutional "in that the said tax is not based upon income and is not in proportion to the population" and that in so far as the collection purported to be based upon official regulations, "it is unconstitutional in that such regulations are beyond the power of the Secretary of the Treasury to promulgate and are beyond the power of Congress to authorize." These allegations at this date raise no serious constitutional question:

> *Brushaber* v. *Union Pacific R. R.,* 240 U. S. 1.
>
> *American Sugar Refining Co.* v. *United States,* 211 U. S. 155.

It is further alleged that the individual members of the Burk-Waggoner Oil Association had by the collection of the tax been subjected to

unlawful and unconstitutional taxation because such taxation was "not authorized by the Revenue Act of 1918 or any other act, and that if it should be held that such taxation was authorized by said act, then that the act is unconstitutional and contrary to the Fifth and Sixth Amendments."

The court below disposed of the first contention (R. 11) by merely citing the Sixteenth Amendment and the cases of *Brushaber* v. *Union Pacific R. R.*, 240 U. S. 1, and *Realty Co.* v. *Anderson,* 240 U. S. 115, and found it unnecessary to consider the second for the reason that the stockholders, for whom the plaintiff was solicitous, were not parties to the litigation, and that the question of the constitutionality of the statute could be raised only by one who alleged that the unconstitutional features injured him, citing *Panama R. R. Co.* v. *Johnson,* 289 Fed. 964. (R. 12.)

The constitutional question, as raised in this Court, may be stated in its last analysis in this way: If the Act be construed as classing with corporations organizations which are in fact partnerships, and imposing upon them the same measure of taxation, it is unconstitutional because Congress has no power to impose income taxes upon partnerships. In other words, if the Act in so many words had imposed the same tax upon "corporations, associations, joint-stock companies, and partnerships," it would have been unconstitutional.

We submit that this contention is wholly unsubstantial. As already pointed out, the Act of October 3, 1917, did impose the war excess-profits taxes upon corporations, including therein joint-stock companies and associations, and also upon partnerships. The excess profits provision of that act was sustained in *LaBelle Iron Works* v. *United States,* 256 U. S. 377, although this precise question was not raised.

After the exposition in *Brushaber* v. *Union Pacific R. R.,* 240 U. S. 1; *Stanton* v. *Baltic Mining Co.,* 240 U. S. 103; and *Realty Co.* v. *Anderson,* 240 U. S. 115, of the power of Congress to impose income taxes since the Sixteenth Amendment, it would seem as if that question had been finally laid at rest.

We submit that the Court may well decline to entertain jurisdiction of this case upon the familiar line of authorities, some of which are cited *supra,* page 2.

CONCLUSION

The judgment should be affirmed or the writ dismissed.

WILLIAM D. MITCHELL,
Solicitor General.
ALFRED A. WHEAT,
Special Assistant to the Attorney General.
OCTOBER, 1925.

○

SUPREME COURT OF THE UNITED STATES.

No. 67.—October Term, 1925.

Burk-Waggoner Oil Association, Plaintiff in Error, *vs.* George C. Hopkins, Collector of Internal Revenue.	In Error to the District Court of the United States for the Northern District of Texas.

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[November 16, 1925.]

Mr. Justice Brandeis delivered the opinion of the Court.

The Burk-Waggoner Oil Association is an unincorporated joint stock association like those described in *Hecht* v. *Malley*, 265 U. S. 144. It was organized in Texas and carried on its business there. Under the Revenue Act of 1918, Act of February 24, 1919, c. 18, 40 Stat. 1057, it was assessed as a corporation the sum of $561,279.20 for income and excess profits taxes for the year 1919. It paid the tax under protest in quarterly instalments, and after appropriate proceedings brought this suit in the federal district court for northern Texas against the Collector of Internal Revenue to recover one of the instalments. The Association asserted that it was a partnership; contended that under the Act no partnership was taxable as such; and claimed that if the Act be construed as authorizing the taxation of a partnership as a corporation, or the taxation of the group for the distributive share of the individual members, it violated the Federal Constitution. The District Court entered judgment for the defendant, 296 Fed. 492. The case is here under § 238 of the Judicial Code, on direct writ of error allowed and filed April 21, 1924. Compare *Towne* v. *Eisner*, 245 U. S. 418, 425.

The Revenue Act of 1918, §§ 210, 211, 218a, 224, 335(c), provides in terms that individuals carrying on business in partnership shall be liable for income tax only in their individual capacity, and that the members of partnerships are taxable upon their distributive shares of the partnership income, whether distributed or not. It subjects corporations to income and excess profits taxes different from those imposed upon individuals. See §§ 210-213,

and §§ 230, 300. It provides in § 1: "That when used in this Act— . . The term 'corporation' includes associations, joint-stock companies, and insurance companies." By the common law of Texas a partnership is not an entity, *Glasscock* v. *Price*, 92 Tex. 271; *McManus* v. *Cash & Luckel*, 101 Tex. 261; an association like the plaintiff is a partnership; its shareholders are individually liable for its debts as members of a partnership, *Thompson* v. *Schmitt*, 114 Tex. —; *Victor Refining Co.* v. *City National Bank of Commerce*, 114 Tex. —; and the association cannot hold real property except through a trustee, *Edwards* v. *Old Settlers' Association* (Tex. Civ. App.), 166 S. W. 423, 426. A Texas statute provides that such associations may sue and be sued in their own name. Act of April 18, 1907, c. 128, Vernon's Sayles' Texas Civil Statutes, 1914, Title 102, c. 2, Arts. 6149-6154. Since the writ of error was allowed, this Court has held in *Hecht* v. *Malley* that associations like the plaintiff are, by virtue of § 1, subject to the special excise tax imposed by the Revenue Law of 1918 on every "domestic corporation".

The Burk-Waggoner Association contends that what is called its property and income were in law the property and income of its members; that ownership, receipt and segregation are essential elements of income which Congress cannot affect; that consequently income can be taxed by Congress without apportionment only to the owner thereof; that the income of an enterprise when considered in its relation to all others than the owners is not income within the purview of the Sixteenth Amendment; and that thus what is called the income of the Association can be taxed only to the partners upon their undistributed shares of the partnership profits, for otherwise such a distribution would neither enrich, nor segregate anything to the separate use of, a partner. The Association further contends that while Congress may classify all recipients of income upon any reasonable basis for the purpose of imposing income taxes at different rates, or for other purposes connected with the levying and collection of such taxes, it cannot tax the income of the Association, for that would make out of a business group, whose property under the law of the State is owned by the members individually, an entity capable of owning property and receiving income; that to attempt this would constitute not classification but an unlawful invasion of the State's exclusive power to regulate the ownership of property within its borders; that, on

the other hand, if the tax be considered as one imposed upon the members and collected from the group, it would likewise be void, both because it is a direct tax not imposed upon income and not apportioned among the States, and because it is so arbitrary and variable in its rates and application as to conflict with the due process clause. The Association contends finally that there is a conflict between the specific provisions of the Revenue Act of 1918 for the taxation of partnership income to the members only and the definition of the term "corporation" in § 1; and that the grave constitutional doubts which necessarily arise, if the Act be construed as attempting to impose the corporation income tax upon associations which by the laws of the State are partnerships, present a compelling reason for construing the Act as not subjecting the Association's income to the taxes imposed upon corporations. Compare *United States* v. *Delaware & Hudson Co.*, 213 U. S. 366, 407.

There is no room for applying the rule of construction urged in aid of constitutionality. It is clear that Congress intended to subject such joint stock associations to the income and excess profits taxes as well as to the capital stock tax. The definition given to the term "corporation" in § 1 applies to the entire Act. The language of the section presents no ambiguity. Nor is there any inconsistency between that section and §§ 218(a) and 335(c), which refer specifically to the taxation of partnerships. The term partnership as used in these sections obviously refers only to ordinary partnerships. Unincorporated joint stock associations, although technically partnerships under the law of many States, are not in common parlance referred to as such. They have usually a fixed capital stock divided into shares represented by certificates transferrable only upon the books of the company, manage their affairs by a board of directors and executive officers, and conduct their business in the general form and mode of procedure of a corporation. Because of this resemblance in form and effectiveness, these business organizations are subjected by the Act to these taxes as corporations.

The claim that the Act, if so construed, violates the Constitution is also unsound. It is true that Congress cannot make a thing income which is not so in fact. But the thing to which the tax was here applied is confessedly income earned in the name of the Association. It is true that Congress cannot convert into a corporation an organization which by the law of its State is

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deemed to be a partnership. But nothing in the Constitution precludes Congress from taxing as a corporation an association which, although unincorporated, transacts its business as if it were incorporated. The power of Congress so to tax associations is not affected by the fact that, under the law of a particular State, the association cannot hold title to property, or that its shareholders are individually liable for the association's debts, or that it is not recognized as a legal entity. Neither the conception of unincorporated associations prevailing under the local law, nor the relation under that law of the association to its shareholders, nor their relation to each other and to outsiders, is of legal significance as bearing upon the power of Congress to determine how and at what rate the income of the joint enterprise shall be taxed.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.